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ENFORCEMENT OF THE COMMUNITY REINVESTMENT ACT

HEARING

BEFORE THE

SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS

OF THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE

ONE HUNDRED FIRST CONGRESS

FIRST SESSION

ON

THE SERIOUS COMPLAINTS FROM CONSUMER GROUPS AND FINANCIAL INSTITUTIONS ABOUT THE REGULATORY ENFORCEMENT OF THE CRA

JULY 31, 1989

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CONTENTS

MONDAY, JULY 31, 1989

Page

Opening statement of Senator Dixon 1

WITNESSES

Griffith L. Garwood, Director of Consumer and Community Affairs, Federal Reserve Board, Washington, DC 3
- Mandate under the CRA 3
- Partnerships 4
- Agency toughness 4
- Prepared statement 6
  - CRA examinations 8
  - Community affairs outreach 10
  - CRA issues in bank expansion proposals 11
  - Supplements to CRA testimony 15
    - 1988 Conferences and Seminars, Attachment A 15
    - Examples of Publications, Attachment B 17
    - Examples of Commitments for Improved Performance, Attachment C 18
    - CRA Examiner Training Hours, Attachment D 24
    - Average Number of Hours Spent on CRA Examinations, Attachment E 25
    - CRA Examination History, Attachment F 26
    - CRA Examination Statistics by Federal Reserve District, Attachment G 27
    - Disposition of Applications, Attachment H 32
- Response to written questions of Senator Dixon 124

Jerauld C. Kluckman, Director of Compliance Programs, Policy Division of the Office of Regulatory Affairs, Federal Home Loan Bank Board, Washington DC 33
- Division of Compliance Programs 33
- Applications 35
- Prepared statement 37
  - FHLB system examination program 37
  - CRA's role in the applications process 43
  - CRA and protested applications 44
  - Shifting CRA's focus from the applications to the enforcement process 46
- Response to written questions of Senator Dixon 139

John H. McDowell, Director of Consumer Activities, Office of the Comptroller of the Currency, Washington, DC 72
- Bank ratings 73
- Prepared statement 75
  - Introduction 75
  - OCC's supervision for CRA 75
  - The OCC's CRA efforts 76
  - CRA ratings by district 77
  - CRA protests 80
  - Other CRA issues 81
  - Summary and conclusion 82
  - Appendix 1. Other OCC activities related to CRA 82
  - Appendix 2. Community Reinvestment Act 86
  - Appendix 3. Uniform interagency CRA rating system 87
- Response to written questions of Senator Dixon 149

Page

Janice M. Smith, Director of Office of Consumer Affairs, Federal Deposit Insurance Corporation, Washington, DC 88
Compliance examination details 88
Monitoring and enforcing 89
Prepared statement 91
Introduction 92
Examination for compliance with CRA 92
The FDIC's examination force 93
Assignment and use of CRA ratings 94
Citizen and community participation 94
Application decisions 95
CRA protests 96
Supervisory enforcement actions 96
Public disclosure of CRA ratings and examination reports 96
Notice of CRA examinations 96
Conclusion 97
Attachments:
1. CRA examination policies and procedures 98
2. Uniform interagency CRA assessment rating system 103
3. Sample FDIC supervisory actions re: CRA 108
Response to written questions of Senator Dixon 161
Panel discussion:
Lack of uniformity between agencies 113
Training program 114
Report language 116
Atlanta investigation 118
Judgment and recommendations 119

ENFORCEMENT OF THE COMMUNITY REINVESTMENT ACT

MONDAY, JULY 31, 1989

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS,
Washington, DC.

The subcommittee met at 2 p.m., in room SD–538 of the Dirksen Senate Office Building, Senator Alan J. Dixon (chairman of the subcommittee) presiding.

Present: Senator Dixon.

OPENING STATEMENT OF SENATOR DIXON

Senator DIXON. This subcommittee meeting will come to order.

Last month, when this subcommittee held a hearing on the Community Reinvestment Act, I heard a clear message. Both consumer groups and financial institutions have serious complaints about the regulatory enforcement of CRA. I announced at the conclusion of that hearing that this subcommittee would hold an oversight hearing about enforcement of CRA. That is our purpose today.

In the intervening time I learned more about the dissatisfaction of both constituencies. Banks all too often are examined by poorly trained examiners who don't quite know what they are looking for, who value different items differently in different years, who spend more energy focusing on formalities of documents than the substance of programs. Banks want clearer standards and firmer timetables, and I don't blame them. The agencies have made some progress recently in some of these areas. We think more is needed.

Community groups, on the other hand, believe that they have borne the burden of enforcing CRA. With inflated grades, a .0025 rate of denied applications, and virtually no real monitoring of the commitments made when an application is approved, I have to agree. Community groups have been the primary force behind CRA, but it is the regulators who should have the resources and the expertise to enforce the law.

Since last month's hearing, I also directed my staff to review on a no-name, confidential basis a range of examination reports in various case files of protested CRA applications. The results have further shown me why CRA, a short, simple statute with few words and one main idea, remains so very contentious. I couldn't tell the difference between reports rated 1 and 2, between 2 and 3, or among 3, 4, and 5. In some reports one couldn't tell at all whether the bank was doing a good job or not. Many of the reports were too

short and quite superficial, and these were reports that regulators selected to show to us.

Protested applications are necessarily messy. Banks and thrifts and their holding companies have a tight timeframe. They want quick regulatory action and view community group objections as a burden, a hindrance, and an unfair intrusion. After all, they feel, the regulators have been handing them satisfactory ratings year after year. Yet, when you examine the records of some of these institutions, they are not taking affirmative steps to help meet the credit needs of low- and moderate-income neighborhoods within their community. They are neglecting certain neighborhoods where working folks who earn modest wages, but pay their bills on time, are good credit risks and potentially profit-generating customers. These institutions are not complying with CRA, but the regulators haven't told them so. The community groups do.

This is not how CRA should work. It is the law of the land that banks and thrifts have an affirmative obligation to help meet the credit needs of the entire community, consistent with safety and soundness. Regulators, not community groups—although I respect and encourage their right to participate—regulators have an affirmative obligation to investigate, to examine whether institutions are living up to the law, and then to impose sanctions when institutions are not.

The March joint statement on CRA is an important step forward by the regulators, and I commend it. We must now make sure that it is implemented and enforced.

I look forward to the testimony of our witnesses today. I hope to learn something from your testimony. I hope you will learn something as well from this hearing. Your testimony claims that the CRA enforcement has been remarkably successful. I cannot say that the community groups, or banks or thrifts, or my colleagues or I would agree. We have noticed, however, important improvements during this year, and I hope that we may work together so that the improvements will continue.

I am delighted to welcome to this subcommittee hearing today Mr. Griffith L. Garwood, Director of Consumer and Community Affairs for the Federal Reserve Board; Mr. Jerauld Kluckman, Director of Compliance Programs in the Policy Division of the Office of Regulatory Affairs, Federal Home Loan Bank Board; Mr. John McDowell, Director of Consumer Activities, Office of the Comptroller of the Currency; and Ms. Janice Smith, Director of the Office of Consumer Affairs, FDIC.

I want you all to know we appreciate your being here today. I understand that my staff has advised you that your full statement will be reproduced in the record. We are delighted to do that, and if each of you could confine your remarks to 10 minutes, it would be greatly appreciated.

Mr. Garwood, we look forward to hearing from you first.

STATEMENT OF GRIFFITH L. GARWOOD, DIRECTOR OF CONSUMER AND COMMUNITY AFFAIRS, FEDERAL RESERVE BOARD, WASHINGTON, DC

Mr. GARWOOD. Thank you, Mr. Chairman. I appreciate this opportunity to address the subcommittee on behalf of the Federal Reserve Board, where I serve as Director of the Division of Consumer and Community Affairs, about our work in enforcing the Community Reinvestment Act.

MANDATE UNDER THE CRA

Our mandate under the CRA is to encourage banks to help meet the credit needs of their entire communities, including low and moderate income areas, to assess their CRA records during examinations, and to take these records into account when evaluating proposals for expansion.

That may sound simple, but it has proven to be most challenging. It requires that we look beyond the bank to its interaction with the people in its community, where rendering an informed judgment requires an understanding not only of banking, but of neighborhoods and the complex forces at work within them.

Our mandate under CRA asks that we encourage banks to be sensitive to CRA concerns, yet quite appropriately, we do not have authority to require them to extend credit under specific terms or in specific amounts. Under CRA institutions have a broad responsibility to their communities, but the law itself provides little practical guidance as to how to measure its fulfillment. It makes CRA performance one of the key factors to be considered in the applications process, but not necessarily a controlling one.

In enforcing the CRA, we have worked to strike a balance between the competing interests and responsibilities of banks and members of their communities. In doing so, we have been criticized by both, as you so appropriately point out. Each side is concerned that we have favored the other, which perhaps is the best indication that we have steered the right course.

We think we have established a sound examination program, directed good education and outreach activities toward the banking community, and used our influence effectively to promote productive bank/community dialog.

I am convinced that the practical result of our efforts and those of others has meant many millions of dollars in the credit extended to low and moderate income neighborhoods and much valuable technical collaboration among all the actors in the CRA process.

In short, I think CRA is working far better than many perceive, not in spite of the regulatory agencies but because we have worked hard to build a solid regulatory framework to carry out our mandate.

With regard to examinations, our specialized examiners regularly conduct CRA assessments, evaluating bank activities and offering suggestions for improvement.

My written testimony explains how examiners look in a detailed, methodical way at bank performance, factoring into their analysis information gained from interviews with business people, Government officials, and community representatives.

I am well aware of the concern about the high incidence of satisfactory CRA ratings, yet I would be surprised if this were not so, given that banks have always had an obligation to serve their communities for reasons of both law and good business.

Moreover, most of the banks we supervise directly are small and are often located in rural areas where links with the community have traditionally been strong.

I would also point out that a 2 rating means that the totality of a bank's efforts to meet the community credit needs is satisfactory and nothing more. In many such cases there may be some room for improvement, and we would bring this to the attention of bank management.

Through our Community Affairs Offices, we share the technical lending expertise banking organizations need to tackle the tougher credit needs in their communities. Educational programs and publications, which I have described in supplements to my testimony, convey this information to thousands of participants each year.

PARTNERSHIPS

To help banks leverage their community investments and make possible even the most complex deals, we have facilitated the formation of partnerships among banks, Government, and private sector organizations. We have also witnessed a heightened interest on the part of the banking community in such initiatives as community development corporations and mortgage loan pools.

In handling applications, the Board carefully reviews the CRA merits of each case, together with financial, competitive, and legal considerations whether or not a protest has been filed. Although we are sometimes criticized for what are thought to be delays caused by CRA protests, we endeavor and are usually able to complete our analysis of cases requiring Board action within a 60-day period. Sometimes it does take longer, particularly if we must seek out additional information from the applicant, the primary regulator, and the protestant, but the fact is that delays in case processing are not the rule, as sometimes suggested.

AGENCY TOUGHNESS

Critics often point to the fact that few cases have been denied on CRA grounds, but this alone is quite misleading as an indication of agency toughness. The Board's longstanding posture has been to take the opportunity afforded by the applications process to encourage banks to do a better job under the CRA.

In attachment C, submitted with my testimony, I have compiled a list of many of the substantive commitments for improvement made by banking organizations in cases where weaknesses were found in their records. This approach has recognized that a limited CRA deficiency may not warrant denial of an application, especially if the other factors the Board must consider weigh in favor of approval. But deficiencies still call for some CRA response. Many communities have gained new or strengthened credit services because of these commitments.

The new interagency CRA policy statement sets out what we have learned to date about effective CRA performance, giving spe-

cific guidance to banks on the types of activities that seem to produce the best results. It makes clear that we expect to see those results. Banking organizations should have their CRA programs in place and working well before filing an application.

This principle was illustrated in the Board's denial of an application by Continental Illinois Bank Corp. in February. The statement puts emphasis on viewing CRA compliance as a process which is an important part of doing business rather than a piecemeal effort to satisfy regulators. It urges banks to open up the channels of communication with people in their communities by, among other things, expanding their CRA statements. By doing this, bankers can take the initiative in telling people what their organizations have done to help meet local credit needs as well as what they plan to do in the future and inviting feedback on those plans.

Just as importantly, the statement encourages community groups to talk to banks about their concerns at an early stage when bankers are best able to respond to them. Our intent here is to promote constructive discussion to the extent possible outside of the high pressure atmosphere of the applications process.

In all of our enforcement activities, examinations, community affairs outreach and the applications processing, we have endeavored to pursue a course which is fair to financial institutions and to the people in the communities they serve and faithful to the mandate given us by the Congress.

Perhaps that effort has not always been perfect, but it has given significant encouragement to private sector participation in community development, and I believe it has made the banking industry very conscious of its CRA responsibilities.

To this extent, I think our efforts can be judged a success. I welcome any questions the subcommittee may have.

[The complete prepared statement of Griffith L. Garwood follows:]

For release on delivery
2:00 p.m., E.D.T.
July 31, 1989

Statement by

Griffith L. Garwood

Director

Division of Consumer and Community Affairs

Board of Governors of the Federal Reserve System

before the

Subcommittee on Consumer and Regulatory Affairs

Committee on Banking, Housing, and Urban Affairs

United States Senate

July 31, 1989

I want to thank the Subcommittee for this opportunity to address issues regarding the Community Reinvestment Act (CRA) and its enforcement by the Federal Reserve. I am pleased to be here to discuss the experience of the Board of Governors of the Federal Reserve System, for which I serve as Director of the Division of Consumer and Community Affairs. The Division's responsibilities include rulewriting and enforcement authority for federal laws safeguarding consumer rights in financial services, especially credit services, in addition to CRA. We oversee and provide policy direction for consumer compliance and CRA examinations performed by Federal Reserve examiners. Through our System-wide Community Affairs Program, we share knowledge about successful approaches to community development lending with bankers. Finally, we analyze and report to the Board on CRA issues which arise in connection with applications.

We have worked hard over the years to develop a multi-faceted program which responds faithfully to our mandate under the CRA. That mandate is three-fold, and can be simply stated: to encourage banks to help meet the credit needs of their entire communities, including low- and moderate-income areas, to assess their records during examinations, and to take their records of service under the CRA into account when evaluating proposals for expansion.

Carrying out that mandate has been anything but simple. In fact, CRA enforcement poses a very significant supervisory challenge in that it compels us to look beyond what happens

within the bank itself, focusing on the role the bank plays in its community. That includes its interaction with individuals, organizations, and local governments to learn about credit needs and its response when such needs are identified. In essence, we must look at a bank's participation in fostering economic growth and revitalization, and making the community a better place to live and to do business. Rendering an informed judgement about that role requires an understanding not only of banking, but of neighborhoods and the often complex social and economic forces at work within them.

Moreover, the statute is framed so broadly that it provides little practical guidance as to appropriate measures of compliance. We have found there is a fine line between encouraging institutions to extend CRA credit and requiring that they do so in specified amounts or types, or under prescribed terms. The Board strongly believes the Congress has not given it authority to establish -- implicitly or explicitly -- lending requirements of any kind under the purview of the CRA. Avoiding such requirements, and still providing both the encouragement which is called for in the Act and the guidance asked of us by many bankers is not an easy task. The Board also must determine what weight to assign to CRA in the applications process, given that it is obliged by law to simultaneously consider financial, managerial, legal, and competitive factors. Factoring the CRA assessment into the mix of these other considerations itself has proved challenging. For central bankers and other financial

regulators, the duties conferred by the CRA require them to wear a "hat" very unlike the traditional one we wear and, quite frankly, this has taken some getting used to.

Nevertheless, in enforcing the CRA we have endeavored to strike a balance between the competing interests and responsibilities of banks and community groups. In so doing, we have been lambasted by both -- which perhaps is the best indication that we have steered the right course. For some years, our actions have been the subject of considerable controversy. Bankers have charged the Federal Reserve with exhibiting bias toward the community organizations, pressuring applicant banks into negotiated settlements with groups filing CRA protests, giving unclear signals about what it takes to "pass" CRA examinations, and unfairly delaying decisions on challenged applications. On the other hand, community organizations have criticized the Federal Reserve for what they perceive to be a "pro-banker" approach to CRA and generally lax enforcement, as well as a reluctance to grant protestants more time to research their case against banks in the context of applications.

Even in this highly controversial setting, it is my belief that the CRA process has been quite positive, which often seems overlooked in the rhetoric which the CRA seems to attract. My remarks here will hopefully convey the extent of our examination effort in which every day on an ongoing basis we send specially trained examiners to call on banks and members of their communities to render CRA assessment and advice. This effort is

augmented by a substantial educational program which has presented new ideas in community economic development to thousands of participants. Through the commitments made by banking organizations in the applications process, a multitude of initiatives has been undertaken. In scores of other instances, private agreements have been reached in the course of CRA-related dialogue between banks and members of their communities.

The practical result of all this activity has probably been many millions of dollars in credit extended in low- and moderate-income neighborhoods, and much valuable, though less quantifiable, technical collaboration among all the actors in the CRA process. It has achieved such results not in spite of the regulatory agencies, as critics allege, but because we have built a solid regulatory framework to carry out our mandate. In short, I believe the CRA process is working far better than many perceive.

CRA Examinations

The cornerstone of CRA enforcement is the CRA examination program, comprehensive in scope yet flexible enough to take into account each bank's asset size and market niche, as well as its locale. CRA examinations are our best vehicle to encourage better performance and will increasingly be the focal point of our enforcement efforts, as indicated in the CRA Policy Statement issued jointly by the agencies in March.

Each state member bank is examined about every 18 months, or more often if weaknesses have previously been identified (and

less often in the case of top-notch performance). The Federal Reserve has long had a cadre of specialized consumer compliance examiners whose training in CRA-related aspects of bank performance sets them apart from other examiners solely concerned with safety and soundness matters. Examiners bring to their jobs a variety of backgrounds in law, accounting, banking and finance. They are trained at Board schools here in Washington, and in regional or Reserve Bank-level seminars. Information about time spent in CRA training, as well as other information responding to specific questions posed by Senator Dixon, is presented in the supplements to this testimony.

Following uniform interagency examination procedures, examiners review and analyze bank activities falling under each of the twelve assessment factors spelled out in Regulation BB. The procedures focus the examiner's attention on each factor in a detailed, methodical way. Through a step-by-step process for each of the factors, examiners build a body of information which, taken as a whole, constitutes the bank's CRA record.

For example, for the assessment factor pertaining to bank marketing and special credit programs, the examiner would review working relationships with realtors servicing low- and moderate-income neighborhoods, efforts in providing mortgage counseling, management assistance to small or minority businesses, the extent to which bank personnel seek out potential housing and small-business loan demand, advertising practices and other matters. Direct lending as well as credit-related services provided in

low- and moderate-income portions of the community would be studied, and compared to lending in more affluent parts of the community. The availability of convenient hours, as well as the accessibility of bank offices to residents of low- and moderate-income areas, would also be considered.

To give breadth and a balanced perspective to the assessment, examiners routinely conduct interviews outside the confines of the bank with business people, government officials, housing and consumer advocates, realtors, trade association representatives and many others. The comments of these individuals -- some 925 of whom were interviewed by Federal Reserve examiners last year -- are factored into the examiners' development of the record.

The examiner's objective is, of course, to evaluate current performance -- but it is also to put banks on a path of strengthened CRA performance. Having the benefit of insight gained from their close, hard look at bank activities and input from community contacts, examiners communicate the findings of their review to bank management orally at the end of the examination, and in written form once they return to the office. They stress areas of weakness and recommend measures for improvement, to which bank management must respond. Continued supervisory attention through correspondence, follow-up visits, and subsequent examinations is given until improvements are realized.

Ratings are assigned in accordance with the uniform interagency CRA rating system which sets out five performance

categories based on the assessment factors. The standards used to measure performance are generally qualitative rather than quantitative in nature, because they must apply to all institutions, in every economic environment. They describe the kinds of programs and practices in which institutions should be engaged to merit ratings on the 1 to 5 scale within each of the performance categories, and on a composite basis. Obviously, assigning ratings involves some judgment on the part of the examiner -- yet this inherent element of judgment does not imply they are arbitrary.

I am well aware of the notion that because the majority of state member banks -- 93% in 1988 and to date in 1989 -- are rated at least satisfactory, something must be wrong. To the contrary, I would be surprised if nearly all banks were not satisfactory, given that the concept of a community service obligation is a bedrock principle of banking. In fact, it has deep historical roots in U.S. banking law, formally enunciated at least as far back as the Banking Act of 1935, which declared that banks should serve the "convenience and needs" of their community. It was reinforced in the Bank Holding Company Act of 1956, which listed the convenience and needs of the community as one of the factors the Board must consider in handling applications under the Act. Numerous state statutes reflect this concept as well.

Particularly with regard to the banks we examine, I would also be surprised if market forces did not work in favor of these

banks which are profitable and are making a strong contribution to the betterment of their communities. Most of the banks directly supervised by the Federal Reserve have total assets under $100 million and/or are located outside metropolitan areas. Small town banks have traditionally been an integral force in their communities and must be sensitive to local concerns, or they would soon be out of business.

One should also bear in mind that we are dealing with a ratings system which gauges performance on a case-by-case basis; we are not seeking to achieve some statistical distribution of high and low ratings around a median. However, for some time the agencies have been undertaking a self-evaluation of our CRA efforts, resulting most recently in the joint policy statement on CRA providing additional guidance on what we believe are effective CRA programs. This review is ongoing and as we learn more I would not be surprised to see an indication in the ratings of somewhat more rigorous measurement.

Community Affairs Outreach

The Community Affairs offices at the Reserve Banks are an important companion to the CRA examination program. It is through these offices that we develop a body of expertise in community development financing, and then share it as widely as possible with banks, bank holding companies, and public sector representatives. We have consistently sought to convey a message of "enlightened self interest," showing how banks can grow and

prosper only together with, and not independent of, the communities surrounding them.

The need for this program became apparent in the very early years of the CRA, when examiners found bankers willing to tackle the tougher credit needs in their communities, but lacking the expertise to make such loans and meet the safety and soundness criteria the law acknowledges. In 1980, we brought to the Division a person experienced in community development lending to provide examiners with information in this field. We soon expanded the program to each of the twelve Reserve Banks.

Last year, community affairs staff conducted over 50 educational programs throughout the country on topics ranging from tax credits for low-income housing to the use of loan pools, loan guarantees and the secondary market. By any measure, I think you will find the list of these programs impressive (Attachment A). Another important resource is the gamut of publications prepared by community affairs staff on the tools and techniques of community development lending. Examples of these are described in Attachment B.

As one outgrowth of these educational efforts, we have witnessed an increasing interest on the part of bank holding companies and national banks in forming subsidiary community development corporations, or CDCs, through which broad investment powers unavailable to banks themselves can be exercised. CDCs can invest in real estate, take equity positions in small businesses and coventure various projects with city, county or

state government and non-profit developers in order to benefit low-income families and poor and blighted communities. In the past 18 months, ten new CDCs have commenced operation.

Given the complexity of inner city redevelopment and rural economic needs, the emphasis in our community affairs program is on forging ongoing relationships between banking and potential partners for development. Over the years a number of partners, besides government, have emerged from such sources as the insurance industry, the philanthropic community, neighborhood-based development corporations and even new national intermediaries such as the Local Initiatives Support Corporation, Neighborhood Housing Services and the Neighborhood Reinvestment Corporation, and the development arm of the National Rural Electric Cooperative Association. These technical and financial partners help banks leverage their community investments and make possible deals that formerly were perceived as "unbankable."

We have done our utmost to promote such partnerships, and have seen worthwhile results. In 1988, for example, a number of California banks formed a consortium to address low-income housing needs. In the Boston district, an affordable housing task force involving lenders, community groups and government officials recently completed a credit needs assessment project. A similarly composed council in Trenton, New Jersey, worked with the Philadelphia Reserve Bank to put together a lenders' profile on that city, together with recommended financing strategies. In Atlanta earlier this year, the Federal Reserve Bank took steps to

encourage the use of the emerging secondary market for community development loans by a coalition of Atlanta mortgage lenders.

The community affairs and CRA examination functions maintain a close working relationship, enabling examiners to keep abreast of new developments in the financial market and to put community affairs staff in touch with bankers in need of technical assistance in CRA matters. I am convinced that our outreach efforts in this area are well placed; judging by the response so far, there is tremendous interest in learning how community development lending can be done to the benefit of banks and their communities.

CRA Issues in Bank Expansion Proposals

Let me now turn to applications processing - an aspect of our work in which there have recently been significant policy developments. The Board is required by law to consider CRA performance when reviewing applications for mergers, acquisitions or branching. While public attention is often drawn to an application in which a CRA protest has been filed, the CRA merits of an application are given careful attention in each case, particularly when any of the banks party to the application have been assigned a less-than-satisfactory CRA examination rating.

Although our focus today is on the CRA aspects of an application, the Board is required by statute to evaluate a number of factors in addition to the convenience and needs.

Protests on any of these grounds -- financial, management, competitive, or CRA -- are viewed seriously, and are handled in exactly the same way. They are thoroughly reviewed by staff and the Board, which sometimes involves seeking out additional information from the applicant, its primary regulator, and the protestant.

Although we endeavor to complete our analysis so that the case can be acted on by the Board within 60 days, we are not always able to meet that target in both CRA and non-CRA cases. Average processing time for the more than 4,000 domestic cases handled by the System in 1987 and 1988 was 39 days. However, the bulk of cases included in that figure -- some 86% -- were decided under delegated authority by the Reserve Banks. Average processing time for the remaining 14% of cases requiring Board action, which would include most CRA cases, was 76 days in 1987, and 72 days in 1988. For CRA-protested applications, average processing time was 73 days in 1987 (somewhat less than the average), and 87 days in 1988 (somewhat more).

One area of controversy has been our practice -- on rare occasions -- of extending the period for receiving comments from protestants. Our policy on extension of the comment period reflects the Board's responsibility to process applications in a timely manner while giving public comments the attention they deserve. Only in a few instances has the Board found extension of the 30-day comment period warranted -- where the application has not been promptly made available for inspection by the

parties, for example, or in the uncommon event there has been inadequate public notice of the application. But it has made clear time and again that it is not appropriate to extend the comment period simply because the commenter wants more time to pursue negotiations with an applicant under the pressure of a pending application.

The agencies' critics often point to the fact that very few applications have been denied on CRA grounds. The Board's longstanding posture has been to utilize the opportunity afforded by the applications process to encourage banks to do a better job under the CRA, though not necessarily through denials. When weaknesses have been found in the record of applicant banks -- whether or not the particular application has been the subject of a CRA protest -- many institutions have made commitments to address them before processing is completed. Those commitments have been taken into account, together with examination reports, comments from the public, and all other information pertinent to an institution's record in coming to a disposition of the application. Roughly one third of the some 150 CRA-protested applications approved involved such commitments. Thus, focusing on the number of applications denied is misleading as the only measure of agency toughness.

Because they address problem areas unique to the case at hand, commitments vary widely. Those made most frequently entail measures such as enhanced advertising and outreach, often in ways that will reach a non-English speaking population; the adoption

of a corporate-wide policy for CRA, accompanied by parent company review of subsidiary activities; and special lending efforts in target neighborhoods. Through this process, dozens of our most prominent banking organizations have made CRA commitments for improved performance. A list of many of the commitments made over the years as part of the applications process is presented in Attachment C.

This approach has recognized that an adverse CRA rating or a limited deficiency in performance may not have warranted denial of the application, particularly if financial, competitive, managerial and legal factors weighed in favor of approval. It also recognized that much could be gained by securing commitments for improved credit services, given that their fulfillment is often monitored through periodic progress reports to Federal Reserve Banks and is taken into account at the time of next application.

I mentioned earlier that the agencies have recently issued a comprehensive CRA Policy Statement. A product of many years of experience with the CRA and the difficult issues it presents, the Statement devotes considerable attention to the role of commitments -- and suggests something of a different direction for the future. It affirms that institutions contemplating business expansion should have CRA policies and programs in place, and working well, before filing an application. While it indicates that commitments for future improvement are entirely appropriate for addressing specific problems in an otherwise satisfactory

record, they cannot compensate for a seriously deficient past record of CRA performance.

This principle was illustrated earlier this year in the Board's denial, in substantial part on CRA grounds, of an application by Continental Illinois Bancorp., Inc., of Chicago, Illinois, to acquire an Arizona bank. The Board acknowledged that Continental had adopted its first formal CRA plan tailored to correct serious CRA shortcomings. Yet in the Board's view Continental's past record, in light of its considerable size and resources, failed to show the basic results on which that plan, which was in very early stages of implementation, could be evaluated. The denial has been well-publicized and, surprisingly, has met sharp criticism from some Chicago community groups -- even before this Subcommittee -- who view the bank's performance from a somewhat different perspective. Nevertheless, the decision stands as a landmark in signaling that institutions should establish a sound CRA performance record before considering expansion.

The joint Policy Statement provides precisely that type of guidance by describing the elements of an effective CRA program. Its key elements are an assertive community outreach program; a means of incorporating information gathered through outreach into the development and refinement of products and services; marketing and advertising which reaches the entire community; periodic analysis of loan applications to ensure that potential borrowers are treated in a fair, equitable manner; and an active

managerial role in CRA planning and oversight. Adopting such a process will help institutions more effectively address their CRA responsibilities as a routine part of doing business.

An important lesson underscored in the course of our enforcement efforts is that communication that begins and ends with a CRA protest rarely brings about long-term benefits. So, as part of routine compliance with CRA, the Policy Statement strongly encourages banking organizations to expand their CRA Statements, expounding on current and future CRA plans and results, to provide a launching point for discussion with the community. At the same time, it encourages neighborhood organizations to react to those expanded CRA Statements, making known their concerns at an early stage when they can be dealt with most effectively by bank management. These comments will be reviewed in the course of the institution's CRA examination. Community members will, of course, continue to be able to submit comments on applications, and each protest will be analyzed carefully and thoroughly.

In all of our CRA enforcement activities -- examinations, community affairs outreach and applications processing -- we have endeavored to be evenhanded toward both financial institutions and representatives of the communities they serve, as well as faithful to the mandate given us by the Congress. Perhaps we have not always done it perfectly, but neither has the effort

been as limited or timid as is sometimes portrayed. We have given significant encouragement to the private sector's participation in community development, and we believe we have made a lasting impression on the way the banking industry views its proper role in the community.

I appreciate this opportunity to speak to the Subcommittee, and welcome any questions you may have.

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Supplements to CRA Testimony

1988 Conferences and Seminars	Attachment A
Examples of Publications	Attachment B
Examples of Commitments for Improved Performance	Attachment C
CRA Examiner Training Hours	Attachment D
Average Number of Hours Spent on CRA Examinations	Attachment E
CRA Examination History	Attachment F
CRA Examination Statistics by Federal Reserve District	Attachment G
Disposition of Applications	Attachment H

ATTACHMENT A

CONFERENCES AND SEMINARS
1988

Established lenders councils in Wilmington, DE, Dayton, Ohio, Camden, New Jersey, Harrisburg, PA, and Philadelphia, PA to develop strategies to address local credit needs.

Cosponsored over 25 meetings for the promotion of Neighborhood Housing Services programs in such cities as Boston, New York, Philadelphia, Richmond, Washington, DC, Dallas, St. Louis, Kansas City, Minneapolis, St. Paul, San Francisco, Los Angeles, and Miami.

Cosponsored with the Small Business Administration a seminar in Denver, Colorado on "Expanding Private Sector Participation in Public Sector Programs."

Cosponsored a conference with the Gulf Coast Economic Development Conference in Beaumont, Texas promoting public/ private partnerships.

Sponsored a seminar in York, PA for community development lenders.

Sponsored small business workshops in Dallas, Austin and El Paso, Texas.

Cosponsored a conference with the Council for Urban Economic Development in Orlando, FL on "Alternative Approaches to Financing Business Development."

Cosponsored a conference with the Federal Home Loan Bank of Cincinnati in Louisville, Kentucky on the opportunities in community development for Kentucky bankers.

Cosponsored a conference in Syracuse, NY and Iselin, New Jersey on "Ten Years of Community Reinvestment."

Cosponsored with the Federal Home Loan Bank of Boston a statewide conference on "Financing Affordable Housing."

Cosponsored a conference with the Federal Home Loan Bank of Seattle, WA in Tacoma, WA on "Community Investment '88."

Cosponsored a conference with the Pitton Foundation and the Denver Partnership in Denver on "Community Development Corporations -- Emerging Options for Community Change."

Sponsored a conference in Midwest City, Oklahoma on Community Development Corporations and the Federal Reserve.

Cosponsored a conference with HUD in Birmingham, AL on "Creative Business Initiatives in the Entrepreneurial American City."

Sponsored a conference in New York on "Community Development Lending -- Building Partnerships for Renewal.

Sponsored a conference in Chicago, IL and Des Monies, IA on "Looking Ahead to 1989: Housing Programs That Work."

Cosponsored with SBA a conference in Grand Junction, Colorado on "Rural Small Business Financing."

Cosponsored a conference with the HUD regional office in El Paso, Texas on community development lending.

Hosted an awards banquet for the 20th anniversary of the original Neighborhood Housing Services of Pittsburgh.

Sponsored a seminar in Detroit on community development lending.

Sponsored a meeting in Savannah, GA on state and federal economic development tools.

Sponsored a meeting in New York for bankers on the rehabilitation program of the New York City's housing department.

Cosponsored a training seminar with the Enterprise Foundation in Baltimore on lending for community development.

Cosponsored a conference in Lubbock, Texas with SBA and Texas Tech on economic development.

Cosponsored with SBA a seminar in Richmond on "International Export Development."

Hosted a seminar for bankers in Houston, Texas on Minority Small Business Investment Corporations.

Sponsored a seminar on consumer and community issues for the Delaware Valley financial institutions in Wilmington, DE.

Cosponsored with the Federal Home Loan Bank of Des Monies, IA a conference in Des Monies on community development lending.

Cosponsored with SBA a seminar in Denver, Colorado on "SBA-Assisted Minority Contracting Programs."

Cosponsored a Lenders Forum in St. Louis with the Federal Home Loan Bank of Des Monies.

Cosponsored with HUD, the State of Virginia and SBA in Richmond a seminar on economic development.

Cosponsored a conference with the Federal Home Loan Bank of Cincinnati in Cincinnati on community development lending and community partnerships.

Sponsored a seminar in Milwaukee, WI on housing programs and public/private partnerships.

Hosted 8 forums of the Northern California Association for Non-Profit Housing in San Francisco.

ATTACHMENT 5

EXAMPLES OF FEDERAL RESERVE COMMUNITY AFFAIRS PUBLICATIONS

"Principles and Practices of Community Development Lending" A bankers "how to" manual for community development lending. Details the steps and decisions involved in the credit analysis of community development projects and offers suggestions for alternate and "gap" financing mechanisms.

"Community Development Corporations and the Federal Reserve" Defines bank holding company community development corporations, their eligible activities, and describes the process of starting a bank holding company community development corporation and receiving approval from the regulator.

"A Bankers Guide to Housing Opportunities for the Poor in Gentrifying Neighborhoods" Discusses the causes of gentrification, how it occurs and what steps banks can take to lessen the impact and remedy the effects of gentrification on a community.

"Mechanisms to Finance Facilities for the Homeless" Discusses available programs and financing solutions for the difficult problem of providing homeless housing in a community.

"Starting a Serious Community Reinvestment Program" Guide for bankers on the steps necessary for starting a successful reinvestment program. This publication offers suggestions for undertaking outreach, performing credit ascertainments, and bank involvement in community development activities.

"Cascade"; "Cross Sections"; "Profitwise"; "Community"; "Community Forum"; "Community Investments" Newsletters which are available from the Federal Reserve System and offer articles on successful community reinvestment programs and current events in community development lending, and banking regulations.

"Options for Investing in Our Communities" Catalog of federal, state and local community development programs focusing on Pennsylvania, Delaware and New Jersey which can be used as a resource in structuring community development projects. Each program listing contains the name and address of the program, a brief program description, a program contact person and a summary of how a bank could utilize the program.

"Opportunities for Community and Economic Development" Separate catalogs for: Arkansas; Illinois; Indiana; Kentucky; Mississippi; Missouri; and Tennessee of federal, state, and local community development programs. Includes program descriptions, contact persons, and information as to how a bank can utilize the program in its community development lending practice.

"Small Business Resource Guide" A listing and description of sources of financing and other services (e.g. technical assistance) available to small businesses in New York State.

"Directory of Community Development Organizations" Listing of community development corporations and other community based organizations located in Massachusetts. This directory can serve as a resource for bankers seeking community contacts for credit ascertainments and marketing efforts or looking for partners in community development projects.

ATTACHMENT C

EXAMPLES OF COMMITMENTS TO THE FEDERAL RESERVE SYSTEM FOR IMPROVING CRA PERFORMANCE 1979-1989

June 1979
Commerce Bancshares, Inc., Kansas City, Missouri

- Advertise residential loans in local neighborhood media
- Increase efforts to assess credit needs
- Periodically meet with protestant

May 1979
Ohio Citizens Trust Company, Toledo, Ohio

- Increase efforts to communicate with members of low- and moderate-income areas

November 1979
Michigan National Corporation, Bloomfield Hills, Michigan

- Improve CRA training of bank personnel
- Participate in special lending programs
- Designate CRA officers

February 1980
Ameritrust Corporation, Cleveland, Ohio

- Improve its training programs for lending personnel to prevent future violations
- Offer credit counseling to applicants or refer them to independent credit counseling organizations
- Make public its real estate appraisal standards
- Study the feasibility of making public its lending policies
- Make the public aware of commitments 2,3 and 4

January 1980
First National Boston Corporation, Boston, Massachusetts

- Increase efforts to establish formal communication channels with local neighborhood groups
- Intensify efforts to upgrade its commitment to extend mortgage credit

June 1980
Manufacturers Hanover Trust Company, New York, New York

- Eliminate policy of not lending on properties with 3- and 4-family units
- Offer long-term, low-downpayment mortgages utilizing private mortgage insurance

December 1980
National City Corporation, Cleveland, Ohio

- Implement an advertising campaign designed to inform lower income groups of available residential credit
- Create and implement a CRA sensitivity program for bank personnel
- Meet more frequently with neighborhood groups

December 22, 1981
AmeriTrust Company, Cleveland, Ohio

Improve strained relations with Protestant and improve communication, by establishing a Community Advisory Council for the Cleveland area.

June 16, 1982
National City Corporation, Cleveland, Ohio

- Meet with Akron Coalition for Community Reinvestment to work out an advertising program designed to reach low- and moderate-income neighborhoods
- Make bank personnel available to counsel community residents on financial matters
- Increase attendance at community meetings
- Encourage input from community groups on how to serve the financial needs of its community, and consider the feasibility of establishing a local community development corporation
- Review CRA efforts in concert with community group

April 1984
Bank of New England Corporation, Boston, Massachusetts

Increase efforts to make community residents more aware of loan programs.

July 1985
Citizens and Southern Corporation, Atlanta, Georgia

Adopt a "Statement of Policy" regarding CRA obligations of its proposed subsidiary banks.

October 1985
First Union Corporation, Charlotte, North Carolina

Adopt formal CRA Undertaking for its proposed subsidiary banks.

November 1985
United Virginia Bankshares, Inc., Richmond, Virginia

Increase lending and other financial services in low- and moderate-income neighborhoods in the District of Columbia.

July 1986
Hibernia Corporation, New Orleans, Louisiana

A six-point CRA enhancement program included:
- Mortgage lending targeted to certain New Orleans neighborhoods, emphasizing FHA and VA loans
- Expanded SBA lending
- Greater advertising of "lifeline" banking services
- More active assessment of credit needs through meetings with community groups, designation of full-time CRA officer, and written instructions to lending staff on CRA matters
- Cashing of government checks at no charge to customers
- Progress reports to the Federal Reserve Bank of Atlanta

August 1986
Marshall & Ilsley Corporation, Milwaukee, Wisconsin

Based on discussions with protestant, M & I committed to undertake several measures in response to community concerns:
- Remove minimum loan amounts in its SBA lending
- Consider "blended rate" business loan offerings in concert with public agencies
- Lower equity requirements for small businesses
- Meet with community groups on a regular basis

Dominion Bancshares Corporation, Roanoke, Virginia

- Expand marketing, with emphasis on underserved neighborhoods
- To the city Council of the District of Colombia, Dominion indicated that it would earmark at least $3 million over the next 5 years for mortgage, home improvement and commercial lending in the District
- Designate responsibility at senior management level for monitoring progress in meeting these commitments

November 1986
Keystone Financial, Inc., State College, Pennsylvania

Keystone committed to fulfill a draft agreement it had proposed to a protestant organization, although the protestant declined to accept it.
- Apply flexible underwriting standards
- Enhance FHA and VA mortgage lending, as well as reduction of mortgage rates and loan origination fees

- Offer credit counseling services
- Enter joint venture partnership with community-based organizations

December 1986
BancOne Corporation, Colombus, Ohio

- Adopt more complete guidelines for CRA compliance by subsidiary banks
- Develop marketing plans to increase loan penetration in low- and moderate-income areas
- Enhance education of bank personnel on CRA, including training in community development lending for loan staff
- Undertake self-evaluation through officer-level CRA Committee
- Make available HMDA data for mortgage banking subsidiary of bank being acquired

May 1987
United Missouri Bancshares, Inc., Kansas City, Missouri

- Include statement stuffers with all checking and savings account statements to improve customers' understanding of home improvement, home purchase and SBA loan products
- Advertise in area newspapers for home improvement, home purchase and SBA loans
- Designate a loan officer to liaise with residents of target neighborhoods
- Better acquaint representatives of mortgage banking subsidiary and the bank to be acquired with Freddie Mac and Fannie Mae requirements
- Conduct training sessions for loan officers and personal banking representatives on CRA
- Display lobby posters and leaflets explaining various loan products and how to apply for them
- Ensure future involvement of the bank being acquired with Old Northeast, Inc., an area neighborhood association, or a similar group
- Make presentations to area groups about bank services
- Submit quarterly reports to the Federal Reserve Bank of Kansas City

April 1987
First Midwest Bancorp, Inc., Naperville, Illinois

Mortgage lending program established in conjunction with a secondary market mortgage service corporation, with goal of sustaining an increased level of mortgage lending. In addition:
- Continue promotion of student loan program to area colleges and universities
- Continue service to small businesses

RepublicBank Corporation, Dallas, Texas

Board noted applicant's agreements with neighborhood groups in Dallas and San Antonio in order to enhance its efforts in those areas calling for:

- Good faith effort to achieve mortgage loan and home improvement loan goals
- Expanded senior citizen checking service
- Marketing plan for target neighborhoods

In addition, Republic will implement its practices and procedures with regard to CRA at all of the banks to be acquired, and will submit a detailed progress report to the Federal Reserve Bank of Dallas.

June 1987
NCNB Corporation, Charlotte, North Carolina

Applicant committed to:

- Designate a Community Affairs Officer for Maryland to meet with community organizations, become familiar with available financing programs, and work with bank officers and lending personnel
- Identify community needs through study of selected low- and moderate-income areas
- Market and advertise more widely in targeted areas
- Endeavor to use flexibility in applying credit criteria
- Provide counseling and technical assistance to governmental and community-based agencies working within the targeted areas
- Develop basic banking services
- Emphasize housing, small business, and economic development loans to targeted areas

September 1987
First Interstate Bancorp, Los Angeles, California

Applicant adopted a corporate CRA policy which establishes a procedure for management review of CRA programs and practices of subsidiary banks. Other actions include:

- Enhance efforts to market housing and small business loans in low- and moderate-income areas
- Increase the number and dollar amounts of loans in low- and moderate-income areas as much as market conditions allow
- Continue to offer basic banking services

October 1987
U.S. Bancorp, Portland, Oregon

To enhance the services of the bank to be acquired, measures include:

- Conduct educational seminars in the South End community of Seattle to provide information about residential and small business loans
- Use price incentives to promote housing and small business loans
- Continued meetings with community organizations
- Establish goals to increase residential real estate and small business lending in the target community

Applicant also adopted a similar plan for the Yakima area.

November 1987
Valley National Corporation, Phoenix, Arizona

To strengthen its CRA performance in certain low- and moderate-income census tracts within Phoenix and Tuscon, Applicant agreed to:

- Strenghten its marketing and consumer education efforts in all segments of its service area
- Expand throughout the state its special lending programs geared to low- and moderate-income persons, especially in rural areas

Meridian Bancorp, Inc., Reading, Pennsylvania

- Develop a plan that addresses credit needs in low- and moderate-income areas of the Philadelphia and Wilmington communities
- Through marketing, increase awareness of special credit programs for residents who do not meet the bank's traditional lending criteria
- Relocate CRA Statements in branch locations to make them more accessible to the public
- More effectively monitor CRA-related efforts and needs throughout the service area
- Expand participation in local reinvestment programs
- Expand the CRA Statement to include special credit programs
- Train branch personnel with respect to the disclosure requirements of HMDA
- Prepare a Spanish CRA notice for use in Hispanic communities in Reading and Philadelphia

October 1987
One National Bancshares, Inc., North Little Rock, Arkansas

- Create full-service residential mortgage lending department with written plan to market real estate loans throughout the delineated community, specifically addressing low- and moderate-income neighborhoods

- Fund FHA, VA and conventional real estate loans and small business loans in low- and moderate-income areas
- Establish comprehensive community outreach program to be coordinated by a Community Service Officer with responsibility monitoring the bank's compliance with CRA and maintaining contact with community organizations

February 1988
The Bank of New York Company, Inc., New York, New York

Bank will reassess its community delineations in New York City, as well as those of the bank being acquired, to ensure they reflect lending territory and do not arbitrarily exclude low - and moderate-income areas. In addition, BONY committed to undertake a CRA plan adopted by its Board of Directors calling for:

- An education and information program for bank officers and employees regarding their responsibilities under CRA and fair lending practices laws
- Designation of a lending officer for each of its principal geographical areas who will be responsible for monitoring the Bank's lending program in that area
- Specialized training to the CRA officer to assist Bank officers and employees in connection with government and community development programs directed at low- and moderate-income communities
- Further broad-based advertising and marketing, including written material in Spanish as well as English
- Periodic meetings with public and private community groups
- Development of loan programs responsive to the credit needs of low- and moderate-income neighborhoods in areas of housing, small business and commercial real estate
- Flexibility, where feasible, in the application of underwriting criteria
- Emphasis on home mortgage and home improvement loans for development and rehabilitation of one-to-four family structures
- Develop CRA compliance reporting and monitoring system, with at least quarterly reports by CRA officers to the Bank's CRA officer and by the Board of Directors

April 1988
SunTrust Banks, Inc., Atlanta, Georgia

With respect to the performance of its Savannah subsidiary, SunTrust will:

- Strengthen consumer compliance by instituting more extensive training and review procedures
- Enhance marketing and credit needs ascertainment efforts in low- and moderate-income and minority neighborhoods
- Through meetings with community representatives and city officials, more aggressively seek out community development financing opportunities
- File quarterly progress reports with the Federal Reserve Bank of Atlanta

May 1988
Saban, S.A., Panama City, Republic of Panama

A comprehensive CRA plan including banking services, housing services, and CRA compliance initiatives, with these key elements:

- Establish extensive community outreach
- Enhance employee CRA training through written communications, formal training, internal publications and quarterly review meetings
- Conduct market analysis to evaluate existing products and address changing needs through introduction of new products
- Promote mortgage products through traditional and targeted advertising
- Work with the New York City housing offices to identify lending opportunities
- Become a SONYMA (state of NY-assisted mortgage program) lender
- Participate in and fund housing development and redevelopment programs
- Submit semi-annual progress reports to the Federal Reserve Bank of New York

June 1988
Norwest Corporation, Minneapolis, Minnesota

- Develop and implement a corporate CRA plan within six months, under which each local bank will prepare a written marketing plan for reaching its entire community
- Set up community advisory boards to help carry out the plan and review each bank's performance
- Provide semi-annual progress reports to the Federal Reserve Bank of Minneapolis

National City Corporation, Cleveland, Ohio

To improve CRA record of Kentucky Bank being acquired, National City will:

- Offer a loan program responsive to housing needs of low- and moderate-income applicants

- Make governmentally-insured loans available, including, FHA, VA, SBA loans
- Offer lifeline banking accounts
- Establish a public policy committee of its Board of Directors responsible for monitoring CRA activities

July 1988
Somerset Bankshares, Inc., Somerville, Massachusetts

- Assign vice president to oversee CRA activities and report regularly to the Board of Directors
- Increase participation in a call program to small businesses
- Meet with local groups involved in housing and credit-related areas
- Enhance advertising of loan products in local media
- More active participation in community development projects
- Provide financial support to a number of state and local housing authorities and community assistance programs
- Submit quarterly progress report to the Federal Reserve Bank of Boston

August 1988
First Bank System, Inc., Minneapolis, Minnesota

In response to CRA examination findings regarding the performance of a Montana subsidiary bank, FBS committed to:

- Establish lending goals and strategies to enhance home mortgage, home improvement, and business lending activities in an economically depressed neighborhood of the bank's community
- Establish outreach and communication channels targeted to this neighborhood
- Invite community group participation in lending programs
- Ensure that its corporate-wide CRA policy is extended to cover all subsidiaries, including the Montana Bank

September 1988
Integra Financial Corporation, Mt. Lebanon, Pennsylvania

- Extend participation in various government lending programs and develop a new mortgage product geared to low- and moderate-income neighborhoods
- Appoint community development affairs officer with duties to report to the Board of Directors on CRA activities
- File semi-annual progress reports with the Federal Reserve Bank and Cleveland

October 1988
Canvest, Inc., Meriden, Connecticut

- Continue efforts to establish a regular pattern of contact with community organizations and government entities
- Continue advertising and regular community contacts to foster greater awareness of credit services
- Continue to seek opportunities to collaborate with government entities, community groups, and/or other financial institutions on community development projects

Comerica Incorporated, Detroit, Michigan

Complete implementation of written CRA plan, developed in conjunction with the Chicago Reserve Bank, with emphasis on:

- More ensurance that Bank's services reach all areas of Detroit and responds to local credit needs
- Increased credit needs ascertainment efforts; in particular, bank will work with community organizations (through seminars, credit surveys, etc.) to develop mortgage lending programs that address the credit needs of low- and moderate-income communities
- Frequent meetings by officers and managers with community groups to discuss credit needs of community
- Increased advertising of home mortgage, home equity, and improvement loan programs
- More active participation in government-sponsored housing-related lending programs
- Quarterly progress reports to the Federal Reserve Bank of Chicago

First Bank System, Inc., Minneapolis, Minnesota

Extend corporate-wide CRA policy to new Colorado subsidiary bank immediately following acquisition

November 1988
Bank of Ireland, Dublin, Ireland

With respect to bank being acquired, applicant will extend its current endeavors:

- Meet the credit and financial needs of the community
- Participate in below-market rate loan programs and offering competitive financing products
- Continue community outreach program involving regular contacts with various community groups

January 1989
FirsTier Financial, Inc., Omaha, Nebraska

Complete implementation of CRA plan to enhance provision of services in Omaha's low- and moderate-income neighborhoods, including:

- Market survey focusing on minority and less affluent parts of the community
- Direct mail advertising campaign in targeted areas
- Appointment of community liaison officer to initiate contacts with community groups
- Development of a computer-based system to track the distribution of credit applications and extensions by census tract
- Pursuant to talks with a protestant organization, FT also pledged to undertake specific lending initiatives, including multi-family housing, mortgage loans for individuals, a secured credit card and a revolving loan fund for home improvement loans

Crestar Financial Corporation, Richmond, Virginia

To supplement its existing CRA plan for the Washington, D.C. area Crestar adopted a "Greater Washington Area CRA Plan" which called for:

- Enhanced advertising and marketing to communicate the availability of credit and other bank services, particularly in minority audience media and neighborhood newspapers
- Participation in local programs and seminars that offer community residents and small businesses technical assistance with respect to obtaining and utilizing credit
- Appointment of CRA Officers at bank, regional and corporate levels with responsibility for carrying out and overseeing CRA performance
- Monitoring CRA performance of all bank subsidiaries
- Meetings between Regional CRA Officers and community leaders to provide feedback from the community

July 1989
Fort Wayne National Corporation, Fort Wayne, Indiana

As an outgrowth of meetings with protestant organization, FW committed to:

- Intensify efforts to identify credit needs in minority and low- and moderate-income segments of its community
- Enhance advertising of special credit programs as well as general credit services

CRA TRAINING HOURS FOR FEDERAL RESERVE SYSTEM EXAMINERS

Schools	1984	1985	1986	1987	1988	1989	Total	
Compliance I								OTHER: Senior Examiner Seminar, 1984
No. Sessions	2	2	2	1	1	2	10	
No. Students	24	40	37	12	19	57	189	18 students
Total Hours	40.5	40.5	40.5	20	20	42	223.5	19 hours
Compliance II								Advanced CRA Training, 1989
No. Sessions	2	1	1	2	1	1*	8	2 sessions
No. Students	26	12	13	25	19	7	102	45 students
Total Hours	11.5	7.5	7.5	16	6.5	8.5	66.5	80 hours
Banking I								
No. Sessions	3	3	4	3	4	2*	19	
No. Students	111	100	166	99	130	50	656	
Total Hours	9	9	12	9	12	6	57	
Banking II								
No. Sessions	3	3	3	4	4	1*	18	
No. Students	84	101	102	141	142	34	604	
Total Hours	9	9	9	12	15	3	57	
BHC Applications								
No. Sessions	2	2	2	2	2	1*	11	
No. Students	43	41	38	36	39	29	226	
Total Hours	2	2	2	2	2	2	12	

* Additional sessions are scheduled for later in the year.

ATTACHMENT E

Federal Reserve System
Average Number of Hours Spent on CRA Examinations

Bank Asset Size (in Millions)	1984	1985	1986	1987	1988
< 25	6	5	5	5	7
25 - 100	7	6	6	7	9
100 - 500	17	14	14	15	13
> 500	44	42	49	72	55

ATTACHMENT F

Federal Reserve System CRA Examination History

	1980	1981	1982	1983	1984	1985	1986	1987	1988 6-30-89
Number of State Member Banks	1011	1046	1060	1075	1075	1096	1108	1092	1081 1073
Number of CRA Reviews	894	894	770	764	709	765	637	598	626 229
Percent Examined For CRA	88%	85%	73%	71%	66%	70%	57%	55%	58% 21%
Average Rating	2.00	1.90	1.97	1.96	1.92	1.90	1.90	1.93	1.99 2.00
Percent Rated Less Than Satisfactory	3%	4%	5%	3%	2%	1%	1%	3%	7% 7%

FEDERAL RESERVE SYSTEM
CRA Examination Statistics: 1984 - 1988

1984	1		2		3		4		5	
	#	%	#	%	#	%	#	%	#	%
Boston	1	14	6	86	0	0	0	0	0	0
New York	10	33	20	67	0	0	0	0	0	0
Philadelphia	1	11	7	78	1	11	0	0	0	0
Cleveland	7	13	43	81	3	6	0	0	0	0
Richmond	10	13	70	88	0	0	0	0	0	0
Atlanta	7	11	55	89	0	0	0	0	0	0
Chicago	3	2	116	93	5	4	1	1	0	0
St. Louis	1	2	44	96	1	2	0	0	0	0
Minneapolis	13	14	75	83	2	3	0	0	0	0
Kansas City	5	5	102	95	0	0	0	0	0	0
Dallas	9	21	34	79	0	0	0	0	0	0
San Francisco	7	12	50	88	0	0	0	0	0	0

ATTACHMENT G

FEDERAL RESERVE SYSTEM
CRA Examination Statistics: 1984 - 1988

1985	1		2		3		4		5	
	#	%	#	%	#	%	#	%	#	%
Boston	2	40	3	60	0	0	0	0	0	0
New York	12	34	21	60	1	3	1	3	0	0
Philadelphia	6	43	8	57	0	0	0	0	0	0
Cleveland	9	17	44	81	1	2	0	0	0	0
Richmond	17	20	65	78	1	1	0	0	0	0
Atlanta	12	15	66	81	2	2	1	1	0	0
Chicago	4	3	142	96	2	1	0	0	0	0
St. Louis	2	4	47	96	0	0	0	0	0	0
Minneapolis	10	14	58	84	0	0	1	1	0	0
Kansas City	1	1	111	99	0	0	0	0	0	0
Dallas	10	19	42	81	0	0	0	0	0	0
San Francisco	8	13	54	86	1	2	0	0	0	0

FEDERAL RESERVE SYSTEM
CRA Examination Statistics: 1984 - 1988

1986	1		2		3		4		5	
	#	%	#	%	#	%	#	%	#	%
Boston	2	33	4	67	0	0	0	0	0	0
New York	9	27	23	70	1	3	0	0	0	0
Philadelphia	4	40	6	60	0	0	0	0	0	0
Cleveland	6	13	38	84	1	2	0	0	0	0
Richmond	7	12	51	88	0	0	0	0	0	0
Atlanta	14	16	70	80	3	3	0	0	0	0
Chicago	2	2	114	97	0	0	1	1	0	0
St. Louis	1	2	42	98	0	0	0	0	0	0
Minneapolis	6	12	43	86	0	0	1	2	0	0
Kansas City	2	3	69	97	0	0	0	0	0	0
Dallas	10	19	43	81	0	0	0	0	0	0
San Francisco	8	13	55	86	1	2	0	0	0	0

FEDERAL RESERVE SYSTEM
CRA Examination Statistics: 1984 - 1988

1987	1		2		3		4		5	
	#	%	#	%	#	%	#	%	#	%
Boston	1	33	2	67	0	0	0	0	0	0
New York	8	29	19	68	1	4	0	0	0	0
Philadelphia	4	36	7	64	0	0	0	0	0	0
Cleveland	6	11	46	87	1	2	0	0	0	0
Richmond	9	12	68	87	1	1	0	0	0	0
Atlanta	2	3	57	85	8	12	0	0	0	0
Chicago	4	3	134	94	5	3	0	0	0	0
St. Louis	2	5	41	95	0	0	0	0	0	0
Minneapolis	6	16	31	82	0	0	1	3	0	0
Kansas City	2	5	40	93	1	2	0	0	0	0
Dallas	9	29	22	71	0	0	0	0	0	0
San Francisco	4	7	56	93	0	0	0	0	0	0

FEDERAL RESERVE SYSTEM
CRA Examination Statistics: 1984 - 1988

1988	1		2		3		4		5	
	#	%	#	%	#	%	#	%	#	%
Boston	3	50	3	50	0	0	0	0	0	0
New York	5	17	20	69	4	14	0	0	0	0
Philadelphia	6	35	10	59	1	6	0	0	0	0
Cleveland	1	3	29	85	3	9	1	3	0	0
Richmond	12	16	65	84	0	0	0	0	0	0
Atlanta	3	3	70	75	19	20	1	1	0	0
Chicago	3	2	118	94	3	2	1	1	0	0
St. Louis	2	5	38	95	0	0	0	0	0	0
Minneapolis	5	12	34	83	1	2	0	0	1	0
Kansas City	3	4	59	84	7	10	1	1	1	0
Dallas	6	17	30	83	0	0	0	0	0	0
San Francisco	6	10	51	88	0	0	1	2	0	0

Disposition of Applications
Handled by Federal Reserve System

1984 - July 1989

	All Domestic Applications	CRA Protested Applications
Total No.	13,600	112*
Approved	12,777	108
Denied	69	1
Withdrawn** or Returned	754	3

* In 32 of these cases, the approval involved commitments for enhanced CRA performance by applicant banks. Performance of these commitments is generally monitored through periodic reporting to Reserve Banks.

** This refers to applications withdrawn by the applicant, which terminates processing of the application. It should not be confused with the withdrawal of a protest by an individual or community group on CRA grounds. There were 38 cases in which CRA protests were withdrawn in this time period.

Senator DIXON. Thank you, Mr. Garwood.
Mr. Kluckman.

STATEMENT OF JERAULD C. KLUCKMAN, DIRECTOR OF COMPLIANCE PROGRAMS, POLICY DIVISION OF THE OFFICE OF REGULATORY AFFAIRS, FEDERAL HOME LOAN BANK BOARD, WASHINGTON, DC

Mr. KLUCKMAN. Mr. Chairman, I am pleased to be here this afternoon to discuss the Federal Home Loan Bank System's regulatory activities associated with the Community Reinvestment Act.

This agency and the industry it regulates has long played a significant role in furthering the housing and community investment objectives of this nation. By their very nature, thrift institutions have been and will continue to be a prominent source of housing finance.

Consequently, CRA will continue to play an important role in efforts to ensure that all individuals have equal access to the credit markets and that financial institutions are meeting community credit needs.

The subcommittee should know that in the past 18 months the Federal Home Loan Bank System has undertaken measures to significantly enhance its overall examination and supervision efforts, including those under CRA. These measures were prompted by the strong commitment of the Board and the System to improve its entire regulatory framework.

As you know, the System struggled through much of the 1980's with staffing and other problems brought on by the well-publicized financial dilemma of the industry and was not able to devote the amount of resources to CRA and a number of other consumer protection laws and regulations as we would have liked.

DIVISION OF COMPLIANCE PROGRAMS

To improve in this area, in October 1987, the Board's Office of Regulatory Activities created the Division of Compliance Programs. This division's purpose is to develop and set national examination policy for consumer protection laws and regulations, such as the Truth in Lending Act, for nondiscrimination statutes, such as the Fair Housing Act and the CRA, and for other public interest laws, such as the Bank Secrecy Act.

In all, the division has responsibility for roughly 20 different laws that fall in the compliance area.

The division has structured much of its work around two broad goals.

First, we believe that our examination program should be balanced with industry education. Because of the complexity of many of the consumer protection laws, we endeavor to provide those we regulate with technical assistance to promote their compliance efforts and instill in those we regulate that compliance is a business responsibility that should be managed as a standard part of operations.

Second, we believe that the System needs to vigilantly regulate the compliance activities of the industry through a comprehensive and consistent examination approach.

Over the past 18 months we have taken five important steps to further our industry education and examination objectives. I would like to highlight these five areas for the subcommittee.

First, in January 1989, the Board approved a specialized examination program for the compliance area. The key elements of the new program are the conduct of separate examinations for compliance performed by trained compliance specialists. A separate comprehensive report of examination is prepared for each specialized examination. Examinations performed under the specialized program utilize separate ratings for overall compliance and for the CRA.

The ratings drive the frequency of future examinations. The interval between examinations for the poorest performance is 6 months, and for the best performers 24 months.

Implementation of the program began in January this year and will be completed by January 1991.

Second, we developed and distributed to agency staff and to the industry a comprehensive compliance activities handbook. This handbook contains information for examiners on the examination process as well as explanations of each law and regulation in the compliance area. It also contains examination objectives, procedures, and checklists. Although the primary audience of the handbook is examiners, thrift institutions should find the handbook useful as an educational tool.

Third, we developed in our Bank System Office of Education a level 1 compliance school for our examiners. That school is going on today, and we are training our first 30 students.

Senator DIXON. How many, did you say?

Mr. KLUCKMAN. Thirty.

Senator DIXON. Thank you.

Mr. KLUCKMAN. Fourth, we developed and distributed to the industry a manual entitled "Compliance: A Self-Assessment Guide." This manual provides guidance for thrift institutions pertaining to the establishment of an internal compliance program and includes information as to the conduct of internal review systems for compliance matters.

Fifth, we developed the compliance assistance series. This is a series of brochures or pamphlets on individual topics that tend to pose problems for thrift institutions. The first brochure, which was recently completed, addressed the Bank Secrecy Act. I have brought along a copy of the new compliance handbook and self-assessment guide and the Bank Secrecy Act pamphlet for the committee's use.

No discussion of the Board's CRA-related efforts would be complete without mentioning and stressing the importance of its community investment activities. The Board's Office of Community Investment and the community investment officers at the Federal Home Loan Banks have since 1978 been providing technical assistance and guidance to thrift institutions, community groups, and State and local officials about investments in local communities.

Through the System's community investment fund—this was a 5-year, $10 billion project—specially priced advances were made to thrifts involved in community investment activities.

In March 1988, the Board reaffirmed its commitment to community investment by the adoption of a housing statement that strongly encouraged the Federal Home Loan Banks to develop programs and support credit policies to assist the community investment efforts of thrift institutions.

APPLICATIONS

I would like to talk about applications for a moment. Applications filed by thrift institutions or their holding companies have historically been infrequent targets of CRA protests by community groups.

The fact that thrift institutions are deeply involved in housing finance, certainly one of the primary objectives of CRA and a strong concern of community organizations, may serve to explain the lack of protest activity.

In the past 5 years the Board has processed only nine protested applications, representing less than one-quarter of 1 percent of all applications.

CRA performance is considered as part of the many types of applications involving federally insured institutions. Unsatisfactory CRA performance is grounds for denying applications.

In the past the Board has used conditional approvals as a way of assuring that an institution improves its CRA performance. Conditions are to be monitored by the district banks and noncompliance with conditions is grounds for denial of future applications or formal enforcement by the Board.

The Board recently denied a branch application on the basis of an institution's failure to satisfactorily meet the terms of a conditional approval it had been granted in connection with a prior application.

Application processing procedures afford the public either a 10 or 20-calendar day period to make comments, depending upon the type of application. These periods will be extended by either 7 or 20 calendar days upon timely request. These comments are considered as part of the applications process.

In addition, the public has a right to make CRA comments about an individual institution's performance, which must be maintained in a public file.

Moreover, our CRA examination procedures have been changed to require examiners to routinely conduct interviews with community organizations and the like as part of the examination process.

Should the Congress decide to require the regulators to make CRA ratings and evaluations public, it is likely that public involvement in the CRA process will greatly increase.

In conclusion, Mr. Chairman, I want to assure you that the Board and the System take our CRA and other consumer protection responsibilities seriously. We have had in existence for some time a program to assist community investment, which is our community reinvestment fund. We have also had programs to identify and eliminate discrimination, such as our complaint handling process and our loan application register system.

We are working diligently to upgrade our examination efforts for these areas, and I believe with the establishment of our examina-

tion specialists we are well on our way to building a sound program.

Thank you.

[The complete prepared statement of Jerauld C. Kluckman follows:]

STATEMENT OF

JERAULD C. KLUCKMAN, DIRECTOR

DIVISION OF COMPLIANCE PROGRAMS, OFFICE OF REGULATORY ACTIVITIES

OF THE FEDERAL HOME LOAN BANK SYSTEM

BEFORE THE SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS

OF THE SENATE BANKING COMMITTEE

JULY 31, 1989

Mr. Chairman, I would like to thank the Subcommittee for the opportunity to testify on the Federal Home Loan Bank System's enforcement of the Community Reinvestment Act (CRA). In response to your invitation letter, my testimony will focus on our compliance examination and enforcement program with particular emphasis on its CRA aspects, the treatment of CRA matters in the applications process, and our experiences with applications protested on CRA grounds.

FHLB System Examination Program

Brief History

Prior to early 1989, the System's CRA and compliance examination responsibilities were carried out as part of the routine safety and soundness examinations of thrift institutions. These examinations were performed by generalist examiners on a 6 to 18 month time frame depending upon the financial condition of an institution. In addition to the overall safety and soundness rating (commonly known as the "MACRO" rating), institutions were assigned a CRA rating. The CRA rating system used a 5-point grading scale, with "1" representing outstanding performance and "5" representing unsatisfactory performance. I will elaborate upon the rating system and the distribution of ratings over the past several years later in this testimony.

Frankly, CRA and other consumer examination responsibilities typically took a backseat to other concerns as the thrift crisis heightened during the mid-1980's, and substantial examination resources needed to be devoted to financial matters. It was not until after 1985 when the examination staff was removed from Civil Service and transferred from the Federal Home Loan Bank Board to the Federal Home Loan Banks that we were able to make plans to enhance our compliance and CRA examination program. We testified

to the Senate Banking Committee on this point twice during 1988. We also testified last year that we were in the process of improving our performance in this important area. I am pleased to be able to tell you that the System has adopted a new compliance examination program and to be able to describe for you the key elements of the new program.

Key Elements of the FHLB System's New Compliance Program

To provide a focus for the development of a national compliance examination program, the System's Office of Regulatory Activities (formerly ORPOS) established the Division of Compliance Programs in October 1987. The primary mission of this division is to develop a national examination and supervisory program to address compliance matters, including CRA. The division's responsibilities include overseeing compliance with the consumer laws and regulations, nondiscrimination requirements, CRA, and a number of other public-interest laws such as the Bank Secrecy Act. A complete description of the program can be found in Exhibit A.

The Division of Compliance Programs has two broad goals. First, the division performs an educational role by assisting member institutions in understanding and complying with laws and regulations. In this regard, the division published a manual entitled, "Compliance: A Self-Assessment Guide" in July 1988. This guide is designed to provide helpful information to an institution in developing a viable compliance program and in conducting and reporting compliance reviews. The guide also includes a policy statement from the Federal Home Loan Bank Board that strongly suggests that every thrift institution establish a compliance program commensurate with its size and complexity. It is the Board's firm belief that it is not only in an institution's best interests to have a viable compliance program, but a business responsibility. A copy of the guide was provided at no cost to member institutions. About 900 copies of the publication have been sold in a little over a year. The division has also

developed a series of brochures addressing regulatory problem areas. The first brochure in the series was devoted to the Bank Secrecy Act and was released in May of this year.

Second, the division administers an enforcement program which directs the System's examination and supervision responsibilities. A separate examination program for the compliance area was approved by the Federal Home Loan Bank Board in January 1989. Probably the most significant element of the new compliance program involves the Board's decision to utilize examiners that specialize in the compliance laws and regulations and CRA. These examiners will receive specialized training in the laws and regulations covered within the scope of the compliance examination.

As a matter of fact, the first Compliance School is being conducted as we speak. The 30 students at this two-week basic school, which began on July 24th, will receive over 20 hours of instruction on the CRA, community investment, nondiscrimination laws and regulations, and applicable examination procedures. Classroom instruction on the CRA and the nondiscrimination laws and regulations is being provided by trained, seasoned professionals with field experience, a staff member from the Board's Office of Community Investment, and a Community Investment Officer from the Federal Home Loan Bank of San Francisco. In addition, on July 26th, a representative from ACORN presented a 1 and 1/2 hour session on the role that community organizations play in the CRA process. Another basic compliance school is slated for December 1989, and two more are planned for 1990 along with an advanced school.

Another significant part of our examiner training regimen includes the division's new Resident Intern Program. Under this program, compliance examiners and other supervisory personnel from the District Banks come to our offices in Washington for a 3-week assignment. During this time, the participant gains an in-depth

education about our functions by becoming involved with special projects, interviewing staff members, and attending interagency meetings and the like. The program began in April of this year and has been very well received by all of the participants so far.

We have also completed and distributed to the staff at the Federal Home Loan Banks and to each thrift institution copies of our "Compliance Activities Handbook." This effort represents the first time that the System has had all of its examination procedures pertaining to the nondiscrimination, consumer, and public interest laws and regulations in a handbook devoted exclusively to them. The new handbook provides examiners with specific guidance as to the conduct of compliance examinations, textual information on each law and regulation contained in the compliance examination program, and examination objectives, procedures, and checklists. In addition to serving as a primary examination tool, the handbook is also an educational centerpiece for institutions.

Examinations under the specialized program are conducted on a frequency schedule driven by the lower of either the CRA or Compliance rating assigned at the previous examination. The interval between examinations can range between 6 and 24 months - the lower the rating, the more frequently an institution would be examined. Ratings assigned during the examination for both CRA and compliance are based on a 5-point scale with "1" representing the most favorable performance and "5" the poorest. Ratings of "1" and "2" reflect satisfactory performance while "3," "4," and "5" signify progressively deepening degrees of unsatisfactory performance. Effective with examinations commencing on or after July 1, 1989, both the Compliance and CRA ratings are being disclosed to an institution's board of directors and management in the examination report.

At the conclusion of a compliance examination, the District Bank prepares a separate, comprehensive examination report written primarily for the benefit of an institution's board of directors and senior management. The report is all narrative and is designed to be consultative and educational. Report content is geared toward areas in need of improvement and is tailored to each individual institution. The CRA Assessment portion of the examination report presents the examiner's evaluation of an institution's compliance with CRA regulatory requirements, and its performance in helping to meet the credit needs of its community pursuant to the CRA examination criteria. The CRA remarks are presented in four subparts: Description of Community Delineation; the twelve CRA Assessment Factors; Violations; and, CRA Conclusions.

The new compliance examination program should be fully staffed and implemented by January 1, 1991. Currently, examiners are being selected and assigned to the compliance area at each District Bank, training is being provided, and separate examination reports are being prepared. The full specialized compliance program may well be completely operational sometime before the 1991 effective date.

CRA Ratings

The CRA rating system requires the examiner to make individual assessments of six CRA performance categories. The performance categories represent groupings of the twelve assessment factors contained in the CRA regulations (12 CFR 563e). Each performance category is evaluated on a grading scale of 1 to 5. In assigning the overall composite CRA rating, the individual performance category assessments are weighed and evaluated according to how well the institution meets the overall descriptive characteristics for that category. The six performance categories are: Community Credit Needs and Marketing; Types of Credit Offered and Extended;

Geographic Distribution; Nondiscrimination Compliance; Other Illegal Credit Practices; and, Community Development and Other Factors.

The CRA rating system employed now is substantially similar to that used by the banking agencies. The Federal Home Loan Bank Board's old CRA rating system basically had 3 "passing grades" in that a "3" rating represented satisfactory performance. Use of the new rating system began with compliance examinations commencing on or after July 1, 1989. A copy of the rating descriptions for the old CRA rating system are in Exhibit B. Copies of the new systems used by examiners for assigning both compliance and CRA ratings are in Exhibit C.

Per your request, the distribution of assigned CRA ratings by Federal Home Loan Bank District from 1983 to 1988 can be found in Exhibit D. This distribution is based on the old CRA rating system. An aggregate between 1983 and 1988 indicates that slightly less than 2 percent of the institutions examined during that period received ratings of either "4" or "5", and 5.4 percent received ratings of either "1" or "2". The overwhelming majority of institutions received a rating of "3", which under the old rating system equated to average performance.

There are a number of reasons that may explain the high percentages of satisfactory ratings. First, thrift institutions have been leading providers of housing finance which is a major CRA-related activity and certainly a primary concern of many community groups. Second, the old rating system spread satisfactory or better performance over 3 rating grades. Third, the relatively low level of CRA protests received throughout the System may indicate general satisfaction with CRA-related activities of thrift institutions.

CRA Examination Procedures

System examiners are directed to use CRA examination procedures that recognize that an assessment of an institution's CRA performance record in helping to meet the credit needs of a local community is a process requiring a balanced viewpoint. The procedures are designed to ensure that information from both the institution and the community are objectively reviewed and evaluated. Each institution is evaluated on the basis of its efforts to ascertain, and its actions to help meet, community credit needs in the context of its resources and local circumstances. A copy of the System's CRA examination procedures is found in Exhibit E.

The objectives of the CRA examination process are straightforward. First, the examiner must determine whether the institution has established and implemented policies and procedures that demonstrate that it has recognized its continuing and affirmative obligation to help meet the credit needs of its entire community and that its facilities serve the credit conveniences and needs of its entire community. Second, the examiner must determine whether the institution's delineation of its local community is in accordance with the regulatory requirements and that the institution is in technical compliance with the CRA regulation.

Specifically, the examiner is charged with evaluating the institution's efforts at ascertaining and meeting community credit needs. Furthermore, the CRA examination procedures now require that examiners routinely interview parties such as real estate brokers, community action groups, religious or political leaders, merchant's organizations, block clubs, neighborhood groups and coalitions, local civil rights, consumer, minority, and non-English speaking groups, housing counseling service centers, community development corporations, nonprofit housing development corporations, and local development corporations. Prior to the

new examination program, these "outside contacts" were made infrequently and usually only when special circumstances were apparent. These interviews enable the examiner to gain a better perspective of the credit needs of the local community as well as an understanding of the extent to which the institution has endeavored to ascertain and meet those credit needs.

In addition to reviewing procedures and conducting interviews, examiners also approach the CRA examination by using a number of other tools. As part of any CRA examination, examiners make use of available HMDA information to determine the geographic distribution of an institution's mortgage loan portfolio. Moreover, they have at their disposal information collected through the Federal Home Loan Bank Board's Loan Application Register/Data Submission Report System (LARS/DSR). This information identifies mortgage lending disparities on prohibited bases from loan application data that are then explored as part of the examination process. The information collected by this system is used to help the examiner evaluate, among other things, an institution's performance under several different CRA assessment factors such as: practices intended to discourage applications for types of credit set forth in the CRA Statement; the geographic distribution of credit extensions, credit applications, and credit denials; and evidence of prohibited discriminatory or other illegal credit practices.

CRA Examination Hours

Exhibit F contains a table that provides a breakdown of CRA examination hours for various asset size ranges of institutions. (Asset size ranges used are: less than $25 million; $25 to $100 million; $100 million to $500 million; and, over $500 million.) Clearly, the table shows that the average examination time spent on CRA increases as the asset size of an institution increases. Between 1983 and 1988, System examiners averaged 3.75 hours per

institution in the smallest shops compared to 16.83 hours on average in the largest ones. The national average for all asset ranges was 7.19 hours.

It is interesting to note that average CRA examination hours have increased significantly in nearly all asset groups since 1986, the year the Board transferred the examiners to the employ of the District Banks. As our new compliance examination program becomes fully operational, we anticipate that more hours will be devoted to the CRA matters.

Joint Statement Regarding the Community Reinvestment Act

On March 21, 1989, the Federal Home Loan Bank Board, along with the other federal financial regulatory agencies with CRA responsibilities, adopted a joint statement regarding the Community Reinvestment Act. The statement is designed to provide federally insured financial institutions and the public with guidance regarding the requirements of the CRA and the policies and procedures the agencies will apply during the applications process to review an institution's CRA compliance and performance. The statement indicates that the CRA examination report will play a significant role in the evaluation process, thus making a strong examination program a prerequisite.

Public Disclosure of Ratings, Examination Evaluations and Notice of Examinations

Ratings and Examination Evaluations

Chairman Wall and Board Member White have indicated by letter to Representative Gonzalez that the agency supports amendments to H.R. 1278 to require the public disclosure of CRA performance ratings and CRA evaluations of institutions. This letter can be

found in Exhibit G. As indicated in that letter, the agency believes, however, that the Congress should give consideration to the public disclosure of a descriptive as opposed to numerical CRA rating so as to not risk confusion with financial soundness ratings.

Notice of Examinations

The System does not believe that providing public notice of CRA examinations is necessary for several reasons. First, the public already has a regulatory right to make comments on any institution's CRA performance. These comments must be maintained by an institution in a public comment file and be readily available for public inspection. In addition, the public has the right to review public comments maintained by the Board or the District Banks. The comments are taken into account as part of the examination process. The public may also file complaints with either the Board or the District Banks. Second, our examiners are now making a more concerted effort to conduct interviews with community groups and organizations as a routine part of the examination. In addition, our examiners will also interview members of the public that have expressed an interest in speaking with an examiner about a CRA concern. Third, the public is notified any time an application is filed by an institution and is invited to submit comments. Fourth, we envision any number of administrative problems that might surface as part of the notification process such as cost associated with newspaper notices, means of notification in rural areas not served, for example, by daily newspapers, and public confusion or concern about safety and soundness of an institution that may result from misinterpreting the intent of the notification. Finally, it appears that Congress will approve the release of CRA ratings and

evaluations, which will increase public involvement in the examination process. Some time should be allowed to observe how that procedure operates before seriously considering an examination notification requirement.

Community Investment Activities

Before turning to a discussion of CRA's role in the applications process, I would like to mention another significant feature of the Federal Home Loan Bank Board's overall approach to furthering the objectives of the CRA. Through the Board's Office of Community Investment and the Community Investment Officers at the Federal Home Loan Banks, the Board has made available to the industry, community groups and state and local officials technical assistance designed to assist thrifts with investments in local communities.

In 1978, the System also established a 5-year, $10 billion Community Investment Fund (CIF). This fund, which has expired, provided $7.9 billion in specially priced advances to thrifts involved in community investment activities. Over 40 percent of our thrift members participated in this voluntary effort that assisted in financing more than 500,000 housing units.

On March 21, 1988, the Board reaffirmed its commitment to a strong community investment program by issuing a policy statement on community investment. This statement urges the Federal Home Loan Banks to develop programs and credit policies to support the community investment efforts of member institutions. The System has responded by the adoption of specially priced Community Investment advances in 10 of our 12 District Banks. To date, over $345 million in CIF advances have been made to member institutions.

CRA's Role in the Applications Process

By legislative direction, CRA performance must be considered by the agencies as part of their disposition of certain types of applications involving federally-insured institutions. Generally, satisfactory CRA performance is a required regulatory criterion in holding company acquisitions, mergers, branching activity, charter conversions, insurance of accounts, change in location and applications involving a change in control. Unsatisfactory CRA performance can be the basis for denial or conditioning of an application.

CRA performance is considered as part of certain holding company acquisitions through the convenience and needs analysis. If the most recent CRA examination rating of an institution controlled by the acquiring entity is less than satisfactory, the acquirer is asked to commit to appropriate corrective actions and reflect those actions in its business plan to the satisfaction of the Board. In the case of mergers between two or more institutions, or branching activities, the most recent CRA examination reports for all entities involved are reviewed. If a merger would create a surviving institution with a less than satisfactory CRA rating, the surviving institution must set forth plans to rectify the CRA deficiencies. To meet the regulatory criteria associated with a change in control application, the institution must have a satisfactory CRA performance record.

Public Notice

The Board requires an applicant to publish a newspaper notice of any application covered by the CRA. The notice must appear in a newspaper of general circulation in the community served by the applicant's home office and in any new locations where the applicant proposes to do business. All notices must contain:

- the applicant's name and location of its home office;
- a description of the type of application;
- the location of any branch office that the applicant proposes to open or relocate;
- the deadline for comments;
- an explanation of the circumstances under which the agency will hear oral arguments about the application;
- instructions about how to submit comments, including the address to which they should be sent.

In the case of a proposed merger, each institution involved must publish a notice. Holding companies must publish a notice in the community served by the home office of any institution the company proposes to acquire. They must also publish a notice in the community served by the home office of the holding company's largest federally-insured subsidiary.

The Federal Home Loan Banks also make notices of applications filed by thrift institutions available to the public in their respective geographic areas upon request. The public is also invited to examine all applications and related documents (subject to certain restrictions) during normal business hours at the appropriate Federal Home Loan Bank.

Public Comments

The public is invited to submit written comments on any application to the appropriate Federal Home Loan Bank as stipulated in the public notice. Generally, comments must be submitted within 10 calendar days after the newspaper notice has

appeared. Requests to make an oral argument must also be submitted within the 10 day period. Seven day extensions of the comment period will be granted to those wishing to protest the application if the request for the extension is made within the initial 10 day comment period. If an application involves a holding company or a change in control, the public has 20 calendar days in which to make comments or protest the application. A 20 calendar day extension will be granted to any person if a request for such is submitted within the initial 20 day period.

CRA and Protested Applications

The Federal Home Loan Bank Board's protest and oral argument procedures are contained in 12 CFR 543.2(e). These procedures apply to applications involving: a change of office location; establishment of a branch office; permission to organize; insurance of accounts; conversion from a State-Chartered institution to a Federally-Chartered institution; merger; and a purchase of branch office or transfer of savings accounts.

"Substantial" Protests

The Principal Supervisory Agent (PSA) at each Federal Home Loan Bank has been delegated the authority to determine whether protests are "substantial." The PSA must make this determination within 10 days of receipt of the protest and so notify the protestant and applicant of his finding. The applicant may submit a rebuttal to any protest up until 10 days after the last date for filing a protest.

A protest is considered "substantial" only if: (1) it is in writing and filed in a timely manner; and (2) the reason for the protest is consistent with at least one of the criteria for denying an application, including CRA. The protest should also contain:

- a summary of the reasons for the protest;
- specific items in the application to which the protestant objects and the reasons for each objection;
- facts supporting the protest, including economic or financial data; and,
- any adverse effects on the protestant which may result from approval of the application.

The FSA's determination on whether a protest is considered "substantial" is considered final. All applications involving "substantial" protests must be forwarded to the Board for action.

Oral Arguments

Any party protesting a merger or branching activity application can ask that a meeting be held for oral arguments on the merits of the application. This request will be granted if the protest is considered "substantial." A District Bank can also decide, absent a request for a meeting, that one be held if it would assist the Board in its evaluation of the application. The meetings are usually held in or near the Federal Home Loan Bank in the applicant's district.

Briefly, either a Supervisory Agent from the local Federal Home Loan Bank or another individual appointed by the Board will preside at the oral argument. Each side is generally given one hour to present their argument. Cross-examination by the parties involved is not permitted. Arguments presented by protestants and applicants must be based on written information already submitted

by either party regarding the application. However, the individual presiding over the meeting may let the parties present new information that is relevant to the written protest. If this is allowed, the opposing party will be given a reasonable time to reply or to submit material in response. A written transcript of the oral argument will be supplied to the applicant and the protestant and be put in the application file that is forwarded to the Board in Washington, D.C.

Analysis and Decision

The Federal Home Loan Bank Board decides all applications involving protests. First, agency staff will review and analyze the application file, the applicant's CRA assessment record, any written protests or comments, the transcript of the oral argument, and any other relevant information. The staff then makes a formal recommendation to the Board for approval or denial of the application based upon its analysis of the entire record. The staff summary of the application, together with its analysis and recommendation, are presented to the Board for decision.

The Board will base its decision on all information available. The Board may either approve or deny the application, or it may approve the application with conditions that the institution will take specific actions to improve its CRA performance.

Protest Activity

Between 1984 and 1988, the System received 9 substantial CRA protests. The Board approved 4 of these protests without conditions and 5 with conditions. (Unfortunately, we have no reliable means of determining the number of withdrawn protests over the 5 year span. 1988 data indicates that 3 protests were withdrawn after the parties reached a settlement). In addition, 3 applications that were not protested were approved with

CRA-related conditions and 2 were denied on CRA grounds. The Board also denied a protested application in 1989. The number of CRA protested applications (9) as a percentage of applications processed (3515) is miniscule. We believe that thrift institutions have not been the subject of much protest activity as a result of their traditional role as providers of housing finance, a major focus of CRA.

Although the Board has an applications tracking system, the average difference in time to process protested versus non-protested applications is not readily accessible. On the basis of our experience, however, it is safe to say that processing time for handling applications protested on CRA grounds is much greater than for non-protested applications.

Conditional Approvals

The Board has used conditional approvals as a means of assuring the future satisfactory CRA performance of an applicant. Compliance with conditions imposed by the Board is monitored by the appropriate District Bank through the normal examination process and through supervisory reviews of institution responses to reporting requirements frequently imposed as part of a condition. If an institution does not fulfill the terms of a condition, the Board can invoke its cease and desist authority, if necessary, to compel the correction of any deficiencies. With the advent of our new compliance examination program, we will be placing emphasis on the monitoring of CRA-related conditions.

Shifting CRA's Focus from the Applications to the Enforcement Process

We would much prefer to see the enforcement of the CRA be more a part of the examination process. We believe that the "Joint Statement of the Federal Financial Supervisory Agencies Regarding the Community Reinvestment Act" makes it clear that an institution's past record, as documented through the examination process and detailed in examination reports, should be given great weight in the applications process. In fact, the Board relied on this factor as one basis for denying an application on CRA grounds on July 19, 1989. Consistent with the joint statement, we also believe that the agency should place, in appropriate circumstances, some weight on commitments offered by an applicant to rectify deficiencies in an otherwise satisfactory CRA performance, and, of course, monitor those commitments.

Shifting CRA's enforcement focus to the examination process would also serve to promote the objectives of CRA among all institutions, not just those who are interested in expansion. With CRA's leverage being limited to the applications process, the law provides little incentive for an institution that does not intend to file a CRA-covered application to aggressively pursue CRA-related activities. This shifting of emphasis, however, cannot take place without a comprehensive examination system. We believe that our new compliance examination program places us in the position to be able to more vigilantly assure that all institutions develop strong CRA programs. We recognize that the applications process is the primary method currently enabling the Board to enforce the CRA and we will continue to use that mechanism together with our enhanced examination program.

In closing, it should be apparent from this testimony that the System has made several significant improvements to its CRA and compliance examination enforcement program over the past 18 months. We are very pleased with the progress we have made but also recognize that our job is not finished. Our new examination program, balanced with our activities aimed at providing industry education and guidance, serve as the keystones of a major thrust to improve our performance in these areas. We take our CRA enforcement responsibilities seriously and fully support the intent and objectives of the law.

EXHIBIT A

SPECIALIZED PROGRAM FOR COMPLIANCE AND TRUST MATTERS

The Federal Home Loan Bank Board has established a new specialized examination program for compliance and trust matters.[1] Implementation of this new program will begin January 1989. The program calls for separate examinations for trust and compliance matters to be conducted by a specialized, dedicated, career-professional examination force. The significant features of this new program are discussed below. The Board is confident that this new program will serve to reinforce the importance that it places on the compliance area and strengthen the System's overall approach to examination and supervision of member institutions.

Significant Features of the New Specialized Program

Generally, the significant features of the new examination program involve the use of specially-trained examination personnel who will conduct separate examinations for the compliance and trust areas. The System will provide these personnel with a specialized training program. Separate reports of examination for each area will be presented to an institution's board of directors. The System will use a separate rating system for each area to evaluate an institution's compliance, CRA, and trust performance. The rating system will provide a mechanism to trigger the frequency of subsequent examinations.

[1] See Attachment A for a detailed listing of the applicable laws and regulations covered by this program.

Handbooks

The Compliance Activities and Trust Activities Handbooks, which are part of the System's Regulatory Handbook Series, embody the written principles and procedures of this new program. In addition to providing materials relevant to the conduct of examinations, the handbooks have a larger role as educational centerpieces for both examiners and member institutions.

Staffing

Each District Bank will have a staff of dedicated specialists whose primary responsibility will be the conduct of compliance and trust examinations. These individuals will be drawn first from the existing examination staff and then from outside sources, and be individuals who have the professional desire, motivation, and capability to handle examinations involving a complex set of dynamic laws, regulations, and fiduciary principles. Individuals who become part of this specialized program will be provided a career path comparable to that for general thrift examiners.

Training

All examination personnel involved in the specialized program will receive training both in the rudiments of the laws and regulations and in examination approach and philosophy. The System will sponsor periodic two-week basic schools for compliance and trust matters, supplemented by one-week secondary level schools. Topical seminars will be conducted periodically as important issues arise.

Examination Conduct

Specialized compliance and trust examinations will be conducted using a "top-down" examination approach. This approach shifts the

examination focus away from individual transactions, to a broad based review of internal policies, procedures, and review programs. This review is supplemented by and evaluation of the integrity of these internal systems through hypothesis testing. This approach is detailed in the Compliance Activities and Trust Activities Handbooks.

Reports of Examination

Separate reports to a member institution's board of directors will be prepared for examinations conducted under this specialized program. These reports will be comprehensive in nature and detail examination findings in a narrative format that gives the reader a thorough analysis of the integrity of the institution's systems and their strengths and weaknesses. These reports will be signed by the person who led the specialized examination.

Ratings

In connection with compliance examinations, examiners will assign two ratings to the institution - one for compliance itself, and one for CRA performance. These rating systems both involve a five point grading scale.

In connection with trust examinations, examiners will assign a rating to the overall trust area. Similarly, this rating system involves the use of a five point grading scale.

Examination Frequency

Both compliance and trust examinations will follow the same basic frequency schedule. The frequency of examinations is primarily dependent upon the rating assigned at the previous examination. The lower the rating, the more frequently the institution is to be examined, thus assuring that limited examination resources are directed to those institutions that are in most need of examination and supervisory attention.

Basically, "1" rated institutions receive a regular examination on a 2-year cycle, with a targeted examination conducted every other 2 years that focuses on new and emerging regulatory trends or requirements as well as the continued reliability of the institution's basic operational systems. Institutions rated "2" receive a regular examination on a 2-year cycle. Institutions rated "3" and "4" receive regular examinations on a 1-year cycle. Institutions rated "5" should receive a regular examination on at least a 6-month interval, as deemed appropriate by the District Bank. Additionally, the District Banks will have the flexibility to extend these intervals in response to unusual circumstances.

Examinations under this specialized program can be conducted concurrently with, or separately from, safety and soundness examinations, at the discretion of each District Bank. Further, a District Bank may decide on the appropriateness of a concurrent or separate examination as circumstances apparent in connection with an individual institution may dictate. In situations where concurrent examinations are conducted, the interval between examinations is to be driven by the lowest rating assigned. For example, if an institution receives a "2" MACRO rating and a "4" compliance rating at a concurrent examination, according to the frequency schedule the next examination would be conducted in one year, the interval that corresponds to a "4" compliance rating.

Organizational Structure

Due to the wide variety of organizational structures present in the District Banks, decisions as to the placement and supervision of the specialized examination function within the District Bank are matters left to local discretion. It is essential, however, that in determining the placement and supervision of the function, special consideration be given to examination scheduling, report review, oversight, quality assurance, technical support and that

appropriate follow-up measures are taken in connection with poorly performing institutions. These duties should be assigned to an individual (with staff as needed) who should be given the necessary responsibility and authority to fulfill them.

Attachment

Laws and Regulations Covered Under the Specialized Examination Program for Compliance and Trust Matters

Compliance

- Bank Secrecy Act
- Bank Protection Act of 1968 (Part 563a)
- Civil Rights Act of 1964
- Civil Rights Act of 1968
- Community Reinvestment Act of 1977
- Delayed Funds Availability Provisions of CEBA - Regulation CC
- Economic Sanctions
- Electronic Fund Transfers Act - Regulation E
- Equal Credit Opportunity Act (including the LARS system)
- Equal Employment Opportunity
- Fair Credit Reporting Act
- Fair Debt Collection Practices Act
- FHLBB Adjustable Rate Mortgage Disclosure Regulations (Parts 545.33, 563.9-9)
- FHLBB Nondiscrimination Regulations (Parts 528, 531.8)
- Flood Disaster Protection Act
- FSLIC Advertising (Parts 563.27, 563.28)
- Home Mortgage Disclosure Act of 1975 - Regulation C
- Interest on Deposits (Part 526)
- Real Estate Settlement Procedures Act of 1974 - Regulation X
- Right to Financial Privacy Act
- Truth in Lending Act - Regulation M (Consumer Leasing)
- Truth in Lending Act - Regulation Z (Truth in Lending, Fair Credit Billing, Unsolicited Credit Card Issuance, Credit Card Solicitation, Home Equity Loan Disclosures)
- Unfair or Deceptive Acts and Practices (Part 535)

Trust

- Trust Powers of Federal Associations (Part 550, 545.102)
- Relevant provisions of the:
- Home Owners Loan Act of 1933 (Section 5(n))
- Employee Retirement Income Security Act of 1974
- Securities Act of 1933
- Trust Indenture Act of 1939
- Securities Exchange Act of 1934
- Internal Revenue Code of 1986

Federal Home Loan Bank Board

Memo

EXHIBIT B

FEDERAL SAVINGS AND LOAN INSURANCE CORPORATION

INTER-OFFICE COMMUNICATION

FROM: Robert J. Moore

DATE: April 18, 1979

TO: Department of Examinations
Professional Staff

SUBJECT: CRA Ratings

Attached for your information and guidance is a copy of a letter sent by the Office of District Banks to the Supervisory Agents. The letter includes some useful guidelines for assigning CRA ratings.

Until formal guidelines are developed and agreed to by all the enforcing agencies please use the attached guidelines in your overall assessments of the performance of associations in regard to CRA.

Robert J. Moore

Deputy Director
Department of Examinations

Attachment

(Letters sent to all District Banks)

Attachment to AB-35

Federal Home Loan Bank Board
Office of District Banks

1700 G Street N.W.
Washington, D.C. 20552

Federal Home Loan Bank Board
Federal Home Loan Mortgage Corporation
Federal Savings and Loan Insurance Corporation

March 30, 1979

Raymond R. Elliott, Supervisory Agent
Federal Home Loan Bank Board
Federal Home Loan Bank of Boston
Post Office Box 2196
Boston, Massachusetts 02106

Re: CRA Ratings

Dear Ray:

As mentioned in my December 15, 1978 memorandum, the Inter Agency Coordinating Committee has determined that each agency will rate institutions' CRA performance on a scale of 1 to 5 based on the examiners' assessment of such performance as set forth in reports of examinations. The "Association Evaluation (Rating)" (Form 648) and the "Transmittal and Analysis Sheet" (Form 168) are being revised to provide for the CRA rating.

The Coordinating Committee decided that only one rating should be assigned based on a given report of examination. For this Agency, this means that while the EIC, District Director and Supervisory Agent will each be required to individually rate an institution's performance, they must all agree on the rating. Should the EIC, District Director or Supervisory Agent be unable to reach agreement on the appropriate rating, the District Director and Supervisory Agent must submit a joint memorandum summarizing the issues to the Deputy Director, Department of Supervision and to the Deputy Director, Field Operations, Department of Examinations for a final decision.

For associations which receive a CRA rating of 4 or 5, there is a need to monitor the associations' progress, or lack thereof, in improving their CRA performance between examinations. Accordingly, the Supervisory Agent, after consulting with the District Director, will be responsible for submitting to the Regional Director a brief memorandum summarizing (a) the factors which led to the 4 or 5 rating, (b) the corrective actions suggested by the examiners or Supervisory Agent to the institution, and (c) the actions, if any, taken or promised by the institution to improve its performance. This written up-date of an institution's performance must be submitted promptly upon completion of the supervisory effort relative to the examination. If this problem is not resolved within 120 days, an

interim status report must be filed with the Regional Director. Should a CRA covered application be filed during this period, it should be held up pending completion of the supervisory effort with respect to CRA matters. Additionally, supervisory clearance of a CRA covered application by an association whose most recent CRA rating was either 4 or 5 must be cleared first with the appropriate Regional Director.

Other than assigning the words "Outstanding", "Good", "Satisfactory", "Needs Improvement" and "Unsatisfactory" to the numerical ratings, the Coordinating Committee has not reached agreement on the criteria to be used in assigning the overall rating. Obviously, the rating must take into consideration each of the twelve factors listed in Section 563e.7. This requires that an institution's performance under one factor be weighed subjectively in terms of its performance under the other factors. However, material violations of the Bank Board's nondiscrimination regulations cannot be mitigated by other CRA performance. Unless corrected, such violations will result in an unsatisfactory rating of 5. Pending the issuance of more specific guidelines by the Coordinating Committee, you may find helpful the following discussion of some of the factors which I believe should be considered in assigning the overall rating.

Outstanding - The association has assumed an active leadership role in furthering the objectives of CRA. This will be usually evidenced by its aggressive efforts acting in concert with various governmental and community groups to identify the special credit needs of its community, particularly in the low/moderate income neighborhoods, and by its efforts in helping to meet such credit needs through a variety of effective, and often innovative, marketing, lending and redevelopment programs. The association normally will have devised prudent programs to help meet the credit needs of its community even in the face of legal or economic impediments and will have committed substantial managerial resources to its efforts.

Good - The association is meeting its obligations under CRA in a positive and aggressive manner. This usually will be evidenced by numerous contacts with community groups and the extent of its affirmative marketing and lending programs. The association for its size and financial condition must have a good record of serving the credit needs of its entire community, particularly in low/moderate income neighborhoods, or it must actively be working to remove roadblocks to such full community involvement.

Satisfactory - The association's community delineation appears reasonable and it has taken steps to identify and help meet the credit needs of its entire community. The association's lending record in its community appears adequate when legal, economic or business grounds are taken into consideration. The association's loan policies and practices must comply with the Bank Board's nondiscrimination regulations. Complaints alleging discrimination or unacceptable CRA performance must have been resolved in the association's favor or the institution must have taken appropriate corrective action.

Needs Improvement - The association's community delineation does not appear consistent with the spirit and intent of CRA and/or the association has taken few, if any, productive steps to identify and help meet the credit needs of its community or the association's efforts are so recent that their probable impact cannot be adequately assessed. The examination report does not disclose any material violation of the Bank Board's nondiscrimination regulation or numerous, repetitive violations of the technical/procedural requirement of the nondiscrimination or CRA regulation. Although the institution cannot fully justify the lack of lending in its community, particularly in low/moderate income neighborhoods, there are clear indications that the institution is becoming increasingly aware of its community responsibilities and that improvements in its CRA performance can be reasonably anticipated.

Unsatisfactory - An association should normally be rated "Unsatisfactory" because of either of the following reasons:

1. The examination report discloses material, unresolved violations of the Bank Board's nondiscrimination regulations or numerous repetitive violations of the technical/procedural requirements of the nondiscrimination or CRA regulations, or

2. The association cannot provide any reasonable justification for its community delineation or its lack of lending in its community, particularly in low/moderate income areas, and material improvements in its CRA performance cannot be reasonably anticipated in light of management's attitude.

If you have any suggestions regarding the foregoing comments, please let us know. Hopefully, we will have time to discuss the CRA rating at our Kansas City meeting on April 10th and 11th.

Sincerely,

James W. McBride
Director

cc: District Director Seaman

Introduction

This section is divided into two parts: Part A – Compliance Rating System, and Part B – CRA Rating System. Unless the scope of an examination is specifically altered to eliminate one phase (e.g., for a special or targeted examination), each compliance examination will address both (1) general compliance with nondiscrimination, consumer protection, and other public interest laws and regulations, except for the Community Reinvestment Act ("CRA"), and (2) performance under the CRA. Separate ratings are given to these two areas, respectively; although the CRA Rating also takes into account the general Compliance Rating with regard to violations of nondiscrimination and consumer credit protection regulations.

The instructions in this section should guide the examiner in assigning appropriate Compliance and CRA ratings, and in developing the narrative rating justifications that will appear in the Confidential Section of the examination report. They will also be useful as a reference throughout the examination and report writing process in regard to determining the relative importance of various findings.

Part A—Compliance Rating System

Background

A uniform, interagency compliance rating system was first approved by the Federal Financial Institutions Examination Council (FFIEC) in 1980. During the next year, the system was adopted by each of the Federal agencies represented on the Council, with the exception of the FHLBS which at the time elected to continue its practice of including consumer compliance as a component of its overall MACRO rating. With the FHLBS's decision to separate consumer compliance examination reports from safety and soundness examination reports, it is appropriate that the ratings also be separated. Therefore, the FHLBS has adopted a Compliance Rating System substantially equivalent to the FFIEC-approved interagency compliance rating system.

The FHLBS Compliance Rating System differs from the interagency version primarily in terms of scope. The range of regulations covered under the term "Compliance" by the FHLBS is somewhat broader than was contemplated, at least initially, by the FFIEC. The FFIEC rating system was designed to reflect, in a comprehensive and uniform fashion, the nature and extent of an institution's compliance with civil rights and consumer protection statutes and regulations. The FHLBB's implementation expands that coverage to encompass compliance with a number of other public interest regulations. Among these are the Bank Secrecy Act, Bank Protection Act, Equal Employment Opportunity, economic sanctions, and advertising.

Since institutions receive separate Community Reinvestment Act (CRA) ratings [see Part B of this Section 110-2], the Compliance Rating System does not include or take into account an institution's performance record with respect to the CRA statute and the Bank Board's implementing regulations. Note also that an institution's performance in the area of trust activities, often referred to as part of the "compliance" arena, is the subject of a separate examination report and rating. For additional information, refer to the FHLBS's Trust Activities Handbook.

The Compliance Rating System is based upon a scale of "1" through "5," in increasing order of supervisory concern. A rating of "1" indicates excellence, while a rating of "5" represents the lowest, most critically deficient level of performance and the highest level of supervisory concern. The Compliance Rating System is a single-value rating system, unlike the MACRO rating which is a composite of several independent ratings of subsidiary elements. The single rating value assigned reflects overall compliance performance, and must be substantiated by the contents of the Report of Examination and the examination workpapers. Characteristics of the five Compliance Ratings available to the examiner are described in greater detail in subsequent paragraphs.

In assigning a Compliance Rating, all factors relevant to compliance with civil rights, consumer protection, and other public interest statutes and regulations must be identified and evaluated. In general, these factors include the commitment of management, as evidenced by its ability and willingness to maintain compliance; the competence of management, as evidenced by the adequacy of operating systems, including internal procedures, controls and audits designed to ensure compliance; and the extent of actual present compliance as a measure of the effectiveness of management's efforts. Other factors unique to specific situations will require attention if the examiner determines they impact significantly upon the overall effectiveness of an institution's compliance efforts.

The primary purpose of the Compliance Rating System is to help identify those institutions whose compliance with civil rights, consumer protection and other public interest statutes and regulations displays weaknesses requiring special supervisory attention and is cause for more than a normal degree of supervisory concern. To accomplish this objective, the rating system identifies a central category of institutions that have compliance deficiencies that warrant more than normal supervisory concern. These institutions are not deemed to present a significant risk of financial or other harm to consumers, but do require a higher than normal level of supervisory attention. Institutions in this category are generally rated "3." Institutions displaying satisfactory and exceptional performance in compliance matters may be rated "2" or "1," respectively. Conversely, institutions whose weaknesses are so severe as to represent, in essence, a substantial or general disregard for the law may be, depending upon the nature and degree of their weaknesses, rated "4" or "5."

The rating categories adopted by the FHLBS for its Compliance Rating System are substantially identical to the categories adopted by other regulators under the FFIEC-approved system. The uniform identification of institutions giving cause for more than a normal degree of supervisory concern will help ensure:

- That the degree of supervisory attention and the type of supervisory response are based upon the severity and nature of the institution's problems;
- That supervisory attention and action are, to the extent possible, administered uniformly and consistently, regardless of the type of institution or the identity of the regulatory agency; and
- That appropriate supervisory action is taken with respect to those institutions whose compliance problems entail the greatest potential for financial or other harm to consumers and the public generally.

Five-Point Compliance Rating Scale

Compliance Ratings are defined and distinguished as follows:

Rating 1

An institution in this category is in a strong compliance position. Management is clearly committed to and capable of, and staff is sufficient for, effectuating compliance. A qualified compliance officer or other specified personnel appropriate for the institution have been given responsibility for compliance assurance, either overall or for specific areas of operations. An effective compliance program, including an efficient system of internal procedures and controls, has been reduced to writing and successfully implemented. The institution provides adequate training for its employees. Changes in relevant statutes and regulations are promptly reflected in the institution's policies, procedures and compliance training. If any violations are noted, they relate to relatively minor deficiencies in forms or practices that are easily corrected. There is no evidence of discriminatory acts, practices, or policies; reimbursable violations; or uncorrected practices resulting in repetition of previously cited violations. Violations and deficiencies are promptly corrected by management. As a result, the institution gives no cause for supervisory concern.

Rating 2

An institution in this category is in a generally strong compliance position. Management is deemed capable of and committed to administering an effective compliance program. Appropriate personnel have been identified as responsible for compliance assurance, and the compliance program reduced to writing. Compliance training is generally satisfactory and conducted routinely to keep staff informed of current requirements. Although the compliance program includes a system of internal operating procedures and controls to ensure compliance, violations have nonetheless occurred. These violations, however, involve technical aspects of the law or result from oversight on the part of operating personnel. Modifications of the institution's compliance and training programs and/or the establishment of additional review/audit procedures should eliminate most of the deficiencies resulting in these violations. There is no evidence of discriminatory acts, practices, or policies; reimbursable violations; or uncorrected practices resulting in a repetition of previously cited violations.

Rating 3

An institution in this category is in a less than satisfactory compliance position. It is a cause for more than normal supervisory concern and requires immediate supervision to remedy deficiencies. Violations, while predominately technical in nature, may be numerous. In addition, previously identified practices resulting in violations may remain uncorrected. However, overcharges, if present, involve only a few consumers and are minimal in amount; and there is no evidence of discriminatory policies or practices. If one or more technical discriminatory acts are found, they are clearly isolated instances inconsistent with the policies and practices of the institution and not indicative of a pattern of discrimination. Although management may have the ability to effectuate compliance, increased commitment and effort are necessary. The numerous violations discovered are an indication that management has not devoted sufficient time and attention to its compliance responsibilities. Operating procedures and controls have not proven effective and require strengthening. This may be accomplished by, among other things, designating a compliance officer, and developing and implementing a more comprehensive, effective compliance program and training effort. By identifying an institution with marginal compliance early, additional supervisory measures may be employed to minimize future violations and prevent further deterioration in the institution's less than satisfactory compliance position.

Rating 4

An institution in this category requires close supervisory attention and monitoring to promptly correct the serious compliance problems disclosed. Numerous substantive as well as technical violations of one or more statutes or regulations are present. Overcharges, if any, affect a significant number of consumers and involve a substantial amount of money. Often, practices resulting in violations and cited at previous examinations remain uncorrected. Discriminatory acts, practices, or policies may be in evidence. Clearly, management has not exerted sufficient effort to ensure compliance. Its attitude may indicate a lack of interest in administering an effective compliance program which may have contributed to the seriousness of the institution's compliance problems. Internal procedures and controls have not proven effective and are seriously deficient. Staff training will generally be found non-existent or haphazard. Prompt action on the part of the supervisory agency may enable the institution to correct its deficiences and improve its compliance position.

Rating 5

An institution in this category is in need of the strongest supervisory attention and monitoring. It is substantially in noncompliance with several of the civil rights, consumer, and public interest statutes and regulations. The severity of its noncompliance creates legal and financial exposure of significant risk to the institution. Management has demonstrated its unwillingness or inability to operate within the scope of these statutes and regulations. Previous efforts on the part of the regulatory authority to obtain voluntary compliance have been unproductive. Discrimination, substantial overcharges or practices resulting in serious repeat violations are present.

Compliance Rating Assessment Guidelines

The Compliance Rating scale has been presented in a narrative format describing the level of compliance for each of the five ratings. When assigning a rating, the examiner should choose the category whose description best reflects the institution's overall compliance position. In many, if not all, cases an institution's compliance posture may not reflect all the factors comprising a single rating category. Consequently, it is important that the extent and types of problems discussed in the examination report support the examiner's rating. The examiner's rating narrative, in the Confidential Section of the examination report, must draw together the import of the various comments presented in the Summary and Findings sections, forming a conclusion that translates into the numerical Compliance Rating to be assigned.

The institution's compliance record and the internal routines and controls used to prevent violations are directly related to management and to the emphasis management places on compliance matters. Therefore, the examiner's rating narrative should commence with a discussion of management. The narrative should then briefly discuss the problem areas within the institution, why the violations occurred, including deficiencies in internal routines and control procedures, and management's proposed corrections. Other matters pertinent to the examination not appropriate for the open report, as well as the names of persons in attendance at the final discussion or board meetings, may be included in the confidential section.

When rating the institution, the examiner should consider and address the topics listed below. A more detailed discussion of these subjects follows.

(a) Management
- ability
- knowledge
- attitude
- succession

(b) Compliance
- nature and extent of violations
- repeat violations
- discriminatory practices and procedures
- overcharges

(c) Internal compliance program
- designation of compliance responsibilities
- audit/review procedures
- training programs

Assessment Guideline Questions

The following questions are meant solely as guidelines for the examiner. Answers to these questions, as well as responses to the examiner's checklists, should aid the examiner in determining the rating and targeting areas for discussion.

Management

Management is the most important component of a well-run organization. Operation of a successful compliance program depends largely upon management's ability, knowledge, and support. Therefore, an analysis of management is essential in determining a rating. When evaluating management, the following should be considered:

Ability:

- Is management technically competent? Does management exert the leadership and administrative abilities necessary to promote compliance with the laws?
- Is management able to interpret (understand) and implement the relevant laws and revisions to the laws? Or, does management rely heavily on the examiners to supply guidance in understanding the laws?
- Does management have the capability of operating the institution within the scope of the regulations? Or, are the problem areas cited in the examination report beyond management's capabilities?

Knowledge:

- Is management familiar with the various civil rights, consumer, and public interest laws and regulations? The content of policy, procedures and training manuals, and the number and type of violations found in the institution, indicate management's knowledge of the laws.
- Does management keep abreast of changes in the laws and regulations? Are training programs instituted to ensure that the institution's staff is informed of the changes?

Attitude:

- Does management have a positive attitude toward regulatory compliance?
- Once identified, are causes of violations promptly corrected, or are there many repeat violations?
- Does management emphasize the importance of compliance with civil rights, consumer and other public interest laws? Designation of appropriate staff with specific responsibilities for compliance assurance, prompt identification and correction of violations and causes of violations, expressed willingness to comply with the regulations, and general responsiveness to supervisory concerns are all indicative of a positive attitude toward compliance.

Management Succession:

- Is there provision for adequate management succession? Although its importance is not limited to compliance matters, management's provision for succession indicates a long range perspective of the institution's future that generally will include a commitment to comply with applicable laws and regulations.

Compliance with the Laws

Violations are indicative of the level of compliance within the institution. The number and types of vio-

lations signal the extent of an institution's problems and are therefore of paramount importance in determining a rating. When rating the institution, the examiner should consider the following:

Nature and extent of violations:

- Are the violations primarily technical in nature and easily corrected? Examples include: failing to include the telephone number of a "required provider" on a good faith estimate; failing to display an "Equal Housing Lender" poster in a branch office; providing the wrong Federal Home Loan Bank address on adverse action notices; omitting the Federal Home Loan Bank address in a Community Reinvestment Act Notice; failing to cross-out old early withdrawal penalty notices placed on the back of CD forms when new penalty notices are given to the consumer.

- Are the violations concerned with practices and procedures that may be more difficult to correct? These violations may have a greater direct impact on the consumer or may subject the institution to liability. For example, the failure to establish separate credit histories or the failure to give rescission notices may directly harm the consumer.

- What is the cause of the violations? Are they the result of established practices and procedures? Is a particular individual primarily responsible?

- How widespread are the violations? Are they restricted to isolated instances?

- Are the violations inadvertent or willful? A violation committed in intentional adherence to an established procedure that is itself in error may be considered inadvertent if (1) creation of the procedural error was inadvertent and (2) the violation is not obvious in its execution and therefore may be carried out with no intention to violate the law.

Types of violations:

- Are the violations substantive?

- Are substantial overcharges and reimbursements involved?

- Are discriminatory practices involved?

- Are there any repeat violations reflecting a continuing policy or practice noted in previous examination reports yet still uncorrected? How often were the violations repeated?

- Are there many violations of the same type, thus constituting a "pattern" of noncompliance?

- What are management's plans for correction? Are these plans likely to correct the cause(s) of the violations?

Internal Compliance Program

Management is directly responsible for the establishment of an effective compliance program. This program will include the designation of compliance responsibilities, assure proper operating procedures and policies, establish a system of internal routines and controls. Such a system may prevent many compliance violations and can usually be implemented with little cost to the institution. Assistance to member institutions wishing to establish or evaluate their internal compliance programs has been provided by the FHLBS in the handbook, "Compliance: A Self-Assessment Guide," distributed by the Office of Regulatory Activities.*

When evaluating the effectiveness of an institution's program, the examiner should focus on its results rather than its specific structure, which may be quite varied between institutions. The following areas should be considered when evaluating internal routines and controls:

Designation of compliance responsibilities:

- Does the institution have a compliance officer?

- If no compliance officer has been formally designated, have specific responsibilities for compliance assurance been assigned to other appropriate members of the staff?

- Is the designated person(s) knowledgeable about the civil rights, consumer, and public interest laws? How much time does this person (s) devote to compliance assurance? How much autonomy does this person(s) possess?

* Copies of the "Guide" may be ordered for $20 prepaid from the Office of Regulatory Activities, Publications, 801 17th St., N.W., Washington, DC 20006.

- If a compliance officer has been designated, has the officer been granted sufficient authority and resources to effectively carry out the functions assigned?

Audit/review procedures:

- Does the institution's audit program include compliance test checks? Are they adequate?

- Does the legal counsel review forms and procedures for compliance?

- Does the institution employ audit/review procedures in its daily work? Does someone recheck forms and calculations for accuracy? Are the files checked to make sure that all necessary forms are complete and that the customer has been given all the correct information?

Training programs:

- Does the institution have an adequate training program? Does the program include training regarding changes in the laws and regulations? Are specific persons responsible for assuring that the training materials are complete and up to date?

- Does the program encompass enough employees, or is it limited to only a few employees?

Additional Comments:

Comments may include subjects that are not detailed specifically elsewhere in the Confidential section. Examples include an anticipated change in certain management positions or ownership of the institution, or the significance of overcharges to capital. If appropriate, comments should also include name of individuals or other sources responsible for substantive violations.

Part B - CRA Rating System

Effective with examinations commenced on or after July 1, 1989, ratings for an institution's performance under the Community Reinvestment Act ("CRA") will be assigned under the revised CRA Assessment Rating System described below. The most significant difference between the Bank System's current CRA rating scale and the new CRA rating scale effective July 1, 1989, is that a "3" rating under the new system indicates CRA performance that, overall, falls short of "satisfactory" due to problems in one or more significant areas. This change makes the "3" of the 5-point CRA rating scale consistent with the "3" of the 5-point scales used by the Bank System in its current MACRO Rating System, and in its new Compliance Rating System and Trust Rating System.

The five gradations of the Bank System's new CRA rating scale are also functionally equivalent to those of the CRA rating system proposed in 1981 by the Federal Financial Institutions Examination Council ("FFIEC"). Thus, implementation of this rating scale will have the added benefit of achieving alignment with the CRA ratings used by the three Federal bank regulatory agencies, all of which adopted the FFIEC system earlier.

Community Reinvestment Act Assessment Rating System

The purpose of this rating system is to provide a comprehensive and uniform system for evaluating and rating the performance of insured member thrift institutions examined under the various assessment factors of the Bank Board's regulations implementing the Community Reinvestment Act.

A CRA rating is assigned to each institution based upon that institution's performance in helping to meet the various credit needs of its local community, including low- and moderate-income neighborhoods, consistent with safe and sound operation. Ordinarily, the CRA evaluation will address performance since the institution's last full CRA examination. In situations where a recently formed entity is being examined, it may be sufficient to assess performance only since the new charter took effect. However, knowledge of the CRA performance of predecessor institutions may be helpful in evaluating performance of the current entity in proper context.

The rating system ranks institutions on a scale from 1 through 5, with a "5" representing the lowest level of performance under the Act and, therefore, the highest degree of concern. Level "3" reflects flawed performance that falls short of satisfactory due to problems in one or more significant areas, although deficiencies are well within management's capabilities to correct if given reasonable attention. Level "1" represents strong, superior performance.

An examiner should begin to evaluate the institution's record in helping to meet community credit

needs by first reviewing its financial condition, size, legal impediments, and local economic conditions, including the competitive environment in which it operates. The type of community in which the institution is located will also have a significant bearing on how the institution fulfills its CRA obligations in the community. Community credit needs will often differ with the specific characteristics of each local community, resulting in a variety of ways an institution may meet those needs. To maintain a balanced perspective, examiners must carefully consider information provided by both the institution and the community.

CRA Rating

The CRA rating is actually a composite developed from individual assessments of six CRA Performance Categories. The Performance Categories represent groupings of the twelve assessment factors contained in the implementing regulation for the Act (12 CFR 563e). Each Performance Category is evaluated on a grading scale of 1 to 5, with a "5" representing the worst performance. These six categories are discussed in the next part.

In assigning the overall composite CRA rating, the individual Performance Category assessments will be weighed and evaluated according to how well the institution meets the overall descriptive characteristics listed below. The six Performance Categories should not be automatically accorded equal weight. Rather, the relative weights applied in order to arrive at the composite rating should be based upon the examiner's understanding of the institution's individual circumstances. In many instances, a particular strength or weakness will directly affect the assessment under more than one Category.

However, an institution found to be in continuing violation of nondiscrimination regulations should normally not receive a composite CRA Rating higher than a "4." A pattern or practice of substantive violations (as defined under Performance Category IV) of nondiscrimination requirements must result in a composite rating of "3." Thus, if the assessment for CRA Performance Category IV is a "4" or "5," that Category will outweigh all other Categories in assigning the composite CRA rating. This emphasis on nondiscrimination compliance as a factor in CRA evaluations continues Bank Board policy implemented in 1979.

CRA Rating (1)

An institution in this group has a strong record of helping to meet community credit needs. Both the board of directors and management take an active part in the process and demonstrate an affirmative commitment to the community. Direct and indirect support of local community reinvestment is viewed as an important aspect of routine operations and policies. Institutions receiving this rating normally place high in all Performance Categories. Such institutions have a commendable record of performance and leadership, and present no supervisory concern in CRA matters.

CRA Rating (2)

An institution in this group has a satisfactory record of helping to meet community credit needs, consistent with its resources and capabilities. Although less aggressive in initiating community contacts and in pursuing special programs than a 1-rated institution, management and the Board of Directors generally consider the objectives of CRA to be an important part of their operations. Institutions receiving this rating normally place in the satisfactory levels of the Performance Categories and present no serious supervisory concern. They may, however, benefit from additional encouragement to help meet community credit needs on an ongoing and more innovative basis.

CRA Rating (3)

An institution in this group exhibits marginal interest in the objectives of CRA and has, overall, an unfavorable record of helping to meet community credit needs. Despite more positive results than evident at a 4-rated institution, the board of directors and management generally do not place strong emphasis on community credit needs in establishing policies and programs. Activities specifically responsive to CRA responsibilities are rarely initiated by the institution without supervisory prompting. Institutions receiving this rating have mixed performance results, surrounding the mid-range levels of the Performance Categories, despite the resources and capability to perform at a higher level. Such institutions require encouragement to help meet the credit needs of their communities.

CRA Rating (4)

An institution in this group is characterized by either a critical decline in CRA performance or, more commonly, a continuing poor record of helping to meet community credit needs. Superficial efforts consistent with CRA objectives, often in response to supervisory criticism, may be evident. Nevertheless, the board of directors and management give inadequate consideration to the credit needs of the institution's community and to compliance with routine requirements of the CRA regulations. Institutions receiving this composite rating generally place poorly in two or more of the Performance Categories, and lack strong compensating performance in the remaining Categories sufficient to achieve an overall rating of (3). Such institutions require strong encouragement to help meet community credit needs. Unresolved deficiencies in regard to nondiscrimination laws and regulations (as indicated by an assessment of "4" under Performance Category IV) may also result in a (4) rating, regardless of satisfactory performance in other CRA categories.

CRA Rating (5)

Institutions in this group have a severely deficient record of helping to meet community credit needs, particularly in low- and moderate-income areas. The board of directors and management appear to give little consideration to the credit needs of the institution's entire community in establishing policies and programs, despite previous supervisory criticism. Institutions receiving this rating generally place at the "4" and "5" levels in most or all Performance Categories. Such institutions require the strongest supervisory encouragement to be responsive to community credit needs. Patterns or practices judged to be substantive violations of nondiscrimination laws and regulations (indicated by an assessment of "5" under Performance Category IV) must result in a (5) rating regardless of performance in other CRA categories.

Performance Categories

Insurance Regulation 12 CFR 563e contains, in addition to CRA regulatory requirements, twelve "assessment factors" that are to be considered in rating an institution's CRA performance. For purposes of this rating system, eleven of the twelve assessment factors listed in section 563e.7 are grouped into six "Performance Categories." The remaining assessment factor, listed in the regulation as factor (k), addresses an institution's ability, or potential, to help meet community credit needs based upon its financial condition, size, legal impediments, local economic conditions, and other similar factors. This factor should be considered in conjunction with each of the six Performance Categories. An institution that performs significantly below its potential, as evaluated under assessment factor (k), should be rated lower in all impaired Performance Categories; whereas legitimate constraints, also recognized under factor (k), should not, of themselves, adversely affect either Performance Category assessments or composite CRA ratings. The six Performance Categories are:

I. Community Credit Needs and Marketing

The institution is evaluated in this fundamental category on its efforts in determining the credit needs of its community and in marketing its services. Included in this category are assessment factors (a), (b), and (c), as well as evaluation of how well the institution delineated its community and of its compliance with requirements for posted notices and maintenance of public files.

II. Types of Credit Offered and Extended

The institution is evaluated in this category on the types and amounts of credit extended throughout its community, and the degree to which those loans are, in fact, helping to meet the community's needs. Included in this category are assessment factors (i) and (j), plus the institution's CRA statement.

III. Geographic Distribution

The geographic distribution of the institution's loans and any practices meant to discourage applications, as well as the impact of the opening or closing of any offices and the services offered at those facilities, are considered in this category. This category covers assessment factors (d), (e), and (g).

IV. Nondiscrimination Compliance

The institution's compliance with nondiscrimination laws and regulations is evaluated in this category. The category addresses the nondiscrimination portion of assessment factor (f).

V. Other Illegal Credit Practices

Compliance with credit protection laws and regulations, excluding the nondiscrimination requirements, is evaluated under this category, which covers the "other illegal credit practices" portion of assessment factor (f).

VI. Community Development and Other Factors

The institution is evaluated in this category on its participation in community development and/or other factors relating to meeting local credit needs. Included in this category are assessment factors (h) and (i).

Performance Category Assessment System

Each of the Performance Categories and the levels of performance relating to each Category are described in greater detail below. Although the CRA assessment factors are grouped here into reasonably related Categories, the factors and groups are not mutually exclusive. Often, a particular strength or weakness will directly affect performance in more than one Category. For example, a weakness in geographic distribution under Category III may relate directly to a weakness in marketing efforts under Category I. In such cases, the examiner should strive for consistency in evaluating actual performance over the full range of Performance Categories.

Where reference is made to types of credit offered, housing, business, and farm credit may be listed with equal emphasis. However, the CRA evaluation should recognize that it is appropriate for thrift institutions to emphasize residential lending over lending for business or farm purposes. In addition, remember to apply the "ability" assessment, factor (k), to each of the six Categories. See Examination Procedure 8 in Section 220 of this Handbook for a detailed description of all twelve CRA assessment factors.

I. Community Credit Needs and Marketing (Assessment Factors (a), (b), (c), Community Delineation and Regulatory Compliance)

- Assessment Level 1

The institution has achieved, and continues to actively and effectively pursue, a comprehensive determination of its community's credit needs. Its activities, conducted to obtain data that is then acted upon by the institution consistent with its CRA responsibilities, may include:

a) identifying the demographic makeup (racial/ethnic groups and low- and moderate-income areas) of its community and making meaningful contacts with a reasonably full range of organizations (civil, religious, neighborhood, minority, etc.) to assist in determining the credit needs of all segments of its community;

b) taking into consideration comments in the public file which describe existing unmet credit needs; or

c) contacting local government officials to identify any needs for private lender participation in existing or prospective community development or redevelopment programs.

The institutionhas actively and effectively undertaken marketing and credit related programs appropriate to the size and capacity of the institution and the nature and location of the community. These programs reach all segments of its community. Community segments would include low- and moderate-income residents and, where applicable, small businesses and small farms. Management has also established working relationships with real estate brokers and others who serve low- and moderate-income areas and who may provide assistance for small or minority businesses. There is evidence that senior management is aware of community concerns and activities. The community delineation is reasonable. No violations of the CRA regulatory requirements are evident.

- Assessment Level 2

The institution has successfully undertaken activities to determine its community's credit needs. As a result of these activities, the institution is generally aware of the credit needs within its community, including low- and moderate-income areas. The institution has initiated a dialogue with community representatives such as local government, neighborhood, religious, and minority organizations, or, as applicable, small business and small farm organizations. The institution has undertaken marketing and credit related programs, including programs in low- and moderate-income neighborhoods, but the programs are not ongoing or comprehensive. Senior management demonstrates an awareness of community concerns and activities. The community delineation is reasonable. Violations of CRA regulatory requirements, if any, were corrected during the course of the examination.

- Assessment Level 3

The institution's activities to determine community credit needs are limited. The institution's employees may serve as volunteers on community organization boards and committees; however, the institution has not established a systematic method to determine how or if its employee's volunteerism assists the institution in meeting its CRA goals. The institution's marketing efforts may be principally deposit oriented. In addition, the institution generally has made no efforts to market its services on an equal basis to all segments of its community. Marketing and credit-related programs do not include a mechanism for reaching low- and moderate-income areas within the delineated community. The institution's marketing effort does not adequately focus on marketing the types of credit for which the institution has identified a need (or for which a need is otherwise apparent). There may also be some concern about the community delineation. Minor violations of CRA regulatory requirements may remain uncorrected at the close of the examination.

- Assessment Level 4

The institution's efforts to determine community credit needs are very limited and fail to address major segments of its community. Management has not established a dialogue with organizations representative of the community, including any which represent low- and moderate-income or minority neighborhoods within the delineated community. The institution's marketing and credit related programs are limited or poorly conceived. Senior management is unaware of special needs of low- and moderate-income residents, small business and small farms. There may also be concern about the community delineation. Violations of CRA regulatory requirements may exist and remain unresolved at the close of the examination.

- Assessment Level 5

The institution has not undertaken any meaningful efforts to determine community credit needs. Management has limited knowledge regarding the community's demographic characteristics. The institution's marketing and credit related programs are either non-existent or have repeatedly excluded low- and moderate-income areas within the delineated community. There may be significant concern about the community delineation. Violations of CRA regulatory requirements may exist and remain unresolved at the close of the examination.

II. Types of Credit Offered and Extended (Assessment Factors (i), (j), and CRA Statement)

- Assessment Level 1

The institution has investigated the need for different types of credit within its community such as residential mortgage loans, housing rehabilitation and home improvement loans, and small business or farm loans, including the need for private, as well as government-insured, guaranteed or subsidized forms of such loans. It has then made an explicit effort to assure that its loan policies are responsive to identified needs, consistent with its resources and capabilities. The CRA Statement accurately and completely describes the types of credit offered. The involvement by the institution in the making of each type of loan listed in its statement demonstrates an affirmative effort in helping to meet existing community credit needs. The institution's CRA Statement may also include some or all of the optional information encouraged by 12 CFR 563e.4(c).

- Assessment Level 2

The institution's CRA Statement and loan portfolio indicate that it has investigated the need for residential mortgage loans, housing improvement/rehabilitation loans, small business and farm loans, and private, as well as government insured, guaranteed, or subsidized forms of such loans within its community. It has made an explicit effort to assure that its loan policies are responsive to the needs found, consistent with its resources and capabilities. The institution's performance in this category is distinguished from a 1-rated institution primarily in the extent to which it is making credit available and/or in the degree to which the types and volume of loans being made match the community's most pressing credit needs.

- Assessment Level 3

The institution may not be offering one or more types of credit listed in its CRA Statement or otherwise identified as being needed in the community, despite the capacity to do so. Loan portfolio analysis or data from other sources may indicate that the institution's volume in a type or types of residential,

small business, or small farm credit needed in the community, including in low- and moderate-income areas, is unjustifiably small relative to demand and the institution's resources. The institution may be underutilizing available private and government insured, guaranteed, or subsidized loan programs to help meet identified credit needs, and can offer no reasonable explanation for failure to take better advantage of these resources.

- Assessment Level 4

The institution's record of offering and of making loans reveals that it is doing relatively little to help meet known or demonstrated credit needs for residential, small business or small farm credit, particularly for residents of low- and moderate-income areas. Its participation in private, as well as government-insured, guaranteed or subsidized loan programs is either perfunctory or nonexistent, under circumstances where the community's need for such loans has been clearly identified and the lender can articulate no objective, supportable reason for its low level or lack of participation. Institution personnel may be poorly trained to pursue increased involvement in private and government sponsored programs. The institution's CRA Statement may be out of date or otherwise inaccurate.

- Assessment Level 5

The institution is unwilling to adapt its credit offerings to serve demonstrated unmet credit needs in its community, particularly for housing, small business or small farm credit, and in low- and moderate income areas. The institution's CRA Statement may be seriously deficient or misleading. This assessment would be particularly appropriate where the lender's failure to meet these needs was cited in a previous examination.

III. Geographic Distribution (Assessment Factors (d), (e), and (g))

- Assessment Level 1

The institution is making its credit products uniformly available to all areas within its community. There is no indication that applicants for any type of credit are being discouraged on the basis of geographical location or any other prohibited basis. The institution periodically reviews the geographic distribution of its credit applications, approvals, and denials. Where that review has disclosed a low level of activity from particular neighborhoods or areas, especially low- or moderate-income areas, the institution has reviewed its marketing practices to determine what, if any, impact they may have had on the distribution. Where appropriate, the institution has revised its marketing practices or lending policies, or both, and has implemented special programs targeting low activity areas. The institution's offices are reasonably accessible to all segments of its community and office hours are tailored to meet the convenience and the needs of its customers. The institution adheres to a stated policy of considering, in advance, the potential impact of opening and closing offices on its ability to offer equal services throughout its community, and of taking special care to avoid, wherever reasonable to do so, reductions in service to low- and moderate-income neighborhoods.

- Assessment Level 2

The geographic distribution of the institution's credit applications, approvals, and denials indicates that the lender is making credit available to all areas within its community. The distribution reveals no patterns suggesting that applications from particular geographical areas are discouraged. Although special marketing programs to target areas of low activity may be minimal, the institution has taken positive steps to address any clearly disparate lending patterns identified previously by examiners or by internal review of credit activity, policies or practices. While no explicit policy may exist, the institution's record of opening and closing offices and the provision of services at its offices do not reflect any adverse treatment of minority or low- and moderate-income neighborhoods. Office facilities and services are reasonably accessible to all segments of its delineated community.

- Assessment Level 3

The geographic distribution of the institution's credit applications, approvals, and denials may suggest possible unreasonable, disparate lending patterns. Management has not recently reviewed its lending policies and procedures or analyzed the institution's lending patterns within its community. There is, therefore, no firm plan in place to explain or otherwise address the questionable patterns. The institution's record of opening and closing offices and its provision for services at its offices may indicate some disparity of treatment between geographical areas within its community, with potentially adverse effect upon low- and moderate-income

neighborhoods. However, such disparity appears to be unintentional, and not an overall pattern or practice. Management readily agrees to address all areas of concern regarding patterns of credit activity and distribution of services.

- Assessment Level 4

The geographic distribution of credit applications, approvals, and denials reveals materially unequal lending patterns, with significantly depressed levels of activity in low- and moderate-income neighborhoods or areas of racial/ethnic concentration. The geographic distribution of applications may indicate prescreening applications or other means of discouraging applicants from certain areas. Management is unable to justify these unequal patterns. The institution's record of opening and closing offices and the provision of services at its offices may suggest a pattern of disparate treatment adverse primarily to minority or low- and moderate-income neighborhoods. The record might portray an institution that has sought to close, or curtail services at, primarily those offices serving minority or less affluent neighborhoods, while opening new offices in developing, non-minority, or upper-income areas. Concerns over credit and/or service patterns or practices raised in prior examinations have resulted in less than adequate responses by the institution.

- Assessment Level 5

The geographic distribution of credit applications, approvals, and denials reveals lending patterns portraying an extensive and systematic avoidance of credit activity in low- and moderate-income or minority areas of the community. The geographic distribution of applications indicates the probability of prescreening applications or otherwise discouraging applicants from certain areas. The institution has adopted, formally or otherwise, loan policies and procedures, such as restrictions based on the age of property (a possible violation of 12 C.F.R. sections 528.2, 528. 2a, and 528.3) or unjustifiably high minimum mortgage amounts or down payments, which have, or can reasonably be expected to have, a measurable adverse effect on loan availability in low- and moderate-income or minority neighborhoods. The institution's record of opening and closing offices and the provision of services at its offices suggest a continuing pattern of disparate treatment adverse to minority or low- and moderate-income neighborhoods. Where current deficiencies were previously cited, meaningful corrective action has not been taken.

IV. Nondiscrimination Compliance (Assessment Factor (f))

The assessement undertaken here should reflect the results of the nondiscrimination portions of the examination. It will, therefore, be necessary to review the workpapers, checklists, and comments developed for those areas. In instances where a CRA Rating is being assigned in the absence of a concurrent full-scope examination, the examiner must make an independent determination of the institution's compliance with nondiscrimination requirements. In any event, the examiner should be alert for indications of prohibited discriminatory practices brought out by the CRA examination procedures that may not have surfaced during the regular examination. If such indications are found, they should be reported inmediately to the EIC or appropriate District Bank supervisor.

For purposes of this assessment, a substantive violation of nondiscrimination laws and regulations is any violation of the Fair Housing Act or the Equal Credit Opportunity Act, or implementing regulations (including provisions of Bank System regulation 12 C.F.R. Part 528), where the institution has used credit criteria in a prohibited discriminatory manner in evaluating an application, has failed to furnish separate credit histories when required, has failed to provide an adequate notice of adverse action, has engaged in prohibited appraisal or advertising practices, or has, on a prohibited basis, discouraged or declined an applicant, required a cosigner or guarantor, or imposed different credit terms.

- Assessment Level 1

The institution is found to be in full compliance with nondiscrimination laws and regulations. It has adopted explicit policy statements supporting nondiscrimination in lending and has implemented strong internal programs to assure its continuing compliance through staff training, written policies and procedures, and internal review and management reporting mechanisms.

- Assessment Level 2

The institution is found to be in satisfactory compliance with nondiscrimination laws and regulations. It

has adopted internal policies and procedures to assure continued compliance, although the program is not as extensive as that cited under Level 1.

- Assessment Level 3

The institution is in less than satisfactory compliance with nondiscrimination laws and regulations. Internal policies and procedures are inadequate to assure compliance. Violations found are sporadic, technical in nature, and do not appear to represent a pattern or practice of prohibited discrimination.

- Assessment Level 4

The institution has an unsatisfactory record of compliance with nondiscrimination laws and regulations. Although a clear pattern or practice of prohibited discrimination may not be indicated, individual violations are numerous and may include a number of substantive violations as well as technical matters. Some violations of non-discrimination laws and regulations cited in past examinations may still be evident.

- Assessment Level 5

The institution is in substantial noncompliance with nondiscrimination laws and regulations. Violations are substantive and numerous, indicative of a pattern or practice of prohibited discrimination in one or more lending activities, or have continued without correction despite previous supervisory criticism.

V. Other Illegal Credit Practices (Assessment Factor (f))

The assessment undertaken here should reflect the results of examination procedures addressing credit protection laws and regulations, other than nondiscrimination (e.g., Truth in Lending, Fair Credit Reporting, Fair Debt Collection, RESPA, and Bank System regulation 12 C.F.R. Part 535). It will, therefore, be necessary to review the workpapers, checklists, and comments developed for those areas. In instances where a CRA Rating is being assigned in the absence of a concurrent full-scope examination, the examiner may generally rely upon findings relevant to this Category presented in the most recent examination report and a brief review to determine whether reported deficiencies, if any, have received corrective attention.

- Assessment Level 1

The institution is found to be in full compliance with credit protection laws and regulations. It has implemented strong internal programs to assure its continuing compliance through staff training, written policies and procedures, and internal review and management reporting mechanisms.

- Assessment Level 2

The institution is found to be in satisfactory compliance with credit protection laws and regulations. It has adopted internal policies and procedures to assure continued compliance, although the program is not as extensive as that cited under Level 1.

- Assessment Level 3

The institution is in less than satisfactory compliance with credit protection laws and regulations. Internal policies and procedures are inadequate to assure compliance. Violations found are sporadic, technical in nature, and do not appear to represent a pattern or practice of noncompliance.

- Assessment Level 4

The institution has an unsatisfactory record of compliance with credit protection laws and regulations. Although a clear pattern or practice of violations may not be indicated, individual violations are numerous. Some violations of credit protection laws and regulations cited in past examinations may still be evident.

- Assessment Level 5

The institution is in substantial noncompliance with credit protection laws and regulations. Violations are substantive and numerous, indicative of a pattern or practice of noncompliance in one or more lending activities, or have continued without correction despite previous supervisory criticism.

VI. Community Development and Other Factors (Assessment Factors (h) and (i))

Note: Under assessment factor (i), an institution may receive favorable consideration for activities that do not fall under the other assessment factors, but which are deemed to help meet the credit needs of its entire community. However, the absence of identifiable "other factors" should not, of itself, be seen as negative.

- Assessment Level 1

The institution has taken affirmative steps to become aware of the full range of community development and redevelopment programs within its community. It is actively participating in the development or implementation of such programs to an extent consistent with its size, capacity, and the nature and location of the community. In non-MSAs, the institution has contacted appropriate government and non-government representatives to determine the level of community development needs in its area. It has then determined what areas are appropriate for its involvement and has initiated such involvement or has undertaken other types of activities not previously covered, which in the examiner's judgment reasonably bear upon the extent to which the institution is meeting the community credit needs.

- Assessment Level 2

The institution is aware of community development/redevelopment programs within its community. It has advised appropriate community officials of its interest in participating in such programs and is already involved in some aspects of program planning or implementation. Or, the institution is planning to undertake a specific activity designed to help meet community credit needs, which has not been covered in other categories, within six months.

- Assessment Level 3

The institution is only vaguely aware of the community development/redevelopment activities in its community. The institution has taken little affirmative action to become involved in community development or to learn the specific features of different programs. Management appears receptive to becoming involved or investing in one or more programs, but prefers to wait for a request to be initiated by community officials. At such time, the institution will consider possible participation. Management has periodically discussed various efforts to respond to community credit needs, but a specific plan has not been developed.

- Assessment Level 4

Management is unaware of the existence or nature of community development programs within its community and has expressed no interest in pursuing this area. Management has not developed any other programs, which were not covered previously, to help meet community credit needs. Management may be unaware of the CRA regulation's encouragement of institution involvement in community development/redevelopment programs.

- Assessment Level 5

Management has repeatedly demonstrated its lack of interest in determining if community development projects exist in its community. It has not expressed an interest in developing its own response to community credit needs.

PAGE 1

EXHIBIT D

AGGREGATE CRA RATINGS
BY DISTRICT
1983

	1	2	3	4	5	TOTAL
01	.	5	77	2	.	84
02	.	5	180	.	.	185
03	.	2	160	.	.	162
04	1	16	307	1	.	325
05	.	12	222	.	.	234
06	.	4	94	.	.	98
07	.	5	250	.	1	256
08	.	6	164	1	.	171
09	.	3	216	1	.	220
10	.	7	85	2	.	94
11	2	6	115	6	.	129
12	.	14	73	1	.	88
*TOTAL YEAR 1983						
	3	85	1943	14	1	2046

AGGREGATE CRA RATINGS
BY DISTRICT
1984

	1	2	3	4	5	TOTAL
01	.	6	53	1	.	60
02	.	5	132	.	.	137
03	.	1	149	.	.	150
04	.	16	291	4	.	311
05	.	8	208	1	.	217
06	.	3	66	2	1	72
07	1	2	221	1	1	226
08	.	.	133	.	.	133
09	.	2	196	2	.	200
10	.	8	135	2	.	145
11	.	4	110	6	.	120
12	.	16	61	1	.	78
*TOTAL YEAR 1984						
	1	71	1755	20	2	1849

PAGE 2

AGGREGATE CRA RATINGS
BY DISTRICT
1985

	1	2	3	4	5	TOTAL
01	.	12	54	1	.	67
02	.	7	148	.	.	155
03	.	3	119	.	.	122
04	.	25	269	4	2	300
05	1	12	189	1	.	203
06	2	.	18	1	.	21
07	2	10	185	2	3	202
08	.	1	178	2	1	182
09	.	3	120	.	.	123
10	.	15	123	3	1	142
11	2	6	83	8	3	102
12	.	8	43	.	.	51
*TOTAL YEAR 1985						
	7	102	1529	22	10	1670

AGGREGATE CRA RATINGS
BY DISTRICT
1986

	1	2	3	4	5	TOTAL
01	.	8	53	1	.	62
02	.	4	167	1	.	172
03	.	2	107	.	.	109
04	.	13	260	4	.	277
05	.	4	193	3	1	201
06	.	3	81	2	.	86
07	.	3	232	1	.	236
08	.	.	137	2	1	140
09	3	18	355	9	10	395
10	.	8	100	.	.	108
11	.	10	128	16	1	155
12	.	13	90	1	.	104
*TOTAL YEAR 1986						
	3	86	1903	40	13	2045

PAGE 3

AGGREGATE CRA RATINGS
BY DISTRICT
1987

	1	2	3	4	5	TOTAL
01	.	15	57	1	.	73
02	.	9	144	1	.	154
03	.	5	136	.	.	141
04	.	13	409	5	2	429
05	.	12	272	2	.	286
06	2	5	131	2	1	141
07	1	6	221	1	2	231
08	.	1	153	3	1	158
09	1	27	220	8	2	258
10	.	18	107	1	.	126
11	.	16	83	7	4	110
12	.	9	81	.	.	90
*TOTAL YEAR 1987	4	136	2014	31	12	2197

AGGREGATE CRA RATINGS
BY DISTRICT
1988

	1	2	3	4	5	TOTAL
01	.	17	34	.	.	51
02	.	8	143	1	.	152
03	.	5	96	.	.	101
04	.	14	319	10	.	343
05	.	9	171	1	1	182
06	.	2	100	2	.	104
07	.	4	215	6	1	226
08	.	.	133	1	1	135
09	3	20	240	10	.	273
10	.	18	66	.	.	84
11	.	21	62	6	5	94
12	.	8	52	2	.	62
*TOTAL YEAR 1988	3	126	1631	39	8	1807

AGGREGATE CRA RATINGS
BY DISTRICT

	1	2	3	4	5	TOTAL
TOTAL	21	606	10775	166	46	11614

EXHIBIT E

Introduction

The Community Reinvestment Act (CRA) is intended to encourage lenders to help meet the credit needs of their entire communities, including low-and moderate-income neighborhoods, while preserving the flexibility necessary for institutions to operate in a safe and sound manner.

The Bank Board is required by the CRA:

- to use its examination authority to encourage an institution to help meet the credit needs of its entire community, consistent with safe and sound operation of the institution.
- to assess, in connection with its examination, an institution's record of helping to meet the credit needs of its entire community.
- to take that record into account in evaluating an application for a charter, deposit insurance, branch or other deposit facility, office relocation, merger, or holding company acquisition of a regulated financial institution.

Proponents of the CRA were concerned, among other things, with situations in which local lenders reportedly exported local deposits to other areas despite sound local lending opportunities. Such disinvestment was considered a threat to community and neighborhood vitality. Lenders are, therefore, encouraged to give increased attention to local housing and development needs of urban and rural areas. Increased lender sensitivity to such lending needs would help preserve, rehabilitate, and revitalize such neighborhoods. Moreover, even though credit for local housing and community development was emphasized, it was realized that other types of credit provide community facilities and services necessary for neighborhood vitality and, more generally, a healthy local community.

CRA is not intended to inject hard and fast rules or ratios into the examination or application processes. Rather, the law contemplates a judgmental evaluation of a lender's record in order to accommodate varying circumstances. Nor does CRA require institutions to make high risk loans that jeopardize their safety. Rebuilding and revitalizing communities are viewed as beneficial for both communities and financial institutions.

CRA Regulation

The regulation requires the board of directors of each institution to adopt and at least annually review a CRA Statement. The statement must include:

- a delineation on a map of each local community served by the institution.
- a list of the specific types of credit that the institution is prepared to extend in each local community.
- a copy of the CRA Notice.

The regulation encourages each institution to also include in its CRA Statement a description of its efforts to ascertain and help meet community credit needs.

An institution must provide in each office a CRA Notice, the exact wording of which is prescribed in the regulation. The public notice indicates that the CRA Statement is available, that written comments on the CRA Statement and the institution's community lending performance may be submitted to the institution or its supervisory agency, that a file of such comments is publicly available, and that the public may request from the supervisory agency, announcements of applications covered by CRA.

Each institution must keep a public file of CRA Statements for the past two years and CRA-related public comments received during the past two years.

The regulation sets forth a list of twelve factors that the agency will consider in connection with its examination in making its assessment of each institution's record of helping to meet community credit needs, including those of low-and moderate-income neighborhoods. The list of factors indicates the kinds of activities to be considered. Institutions are not required to adopt particular activities on the list since the regulation is designed to allow each institution considerable flexibility in determining how it can best help to meet the needs of its entire community in view of its particular skills and resources.

The assessment of an institution's CRA record will be taken into account in evaluating a variety of applications by the institution.

In essence, the regulation encourages institutions to become aware of the full range of credit needs of their communities and to offer the types of credit and credit-related services that will help to meet those needs. However, the regulation does not require institutions to offer particular types or amounts of credit.

Background for Examinations

General

In connection with examinations, the Bank Board is required to assess an institution's CRA record. The examiner plays a major role in this assessment process, with other personnel such as supervisory agents, community investments officers and applications staff using the examiner's findings in making judgments on applications.

Judgmental Process

Community credit needs differ somewhat with the specific characteristics of each local community, and institutions may serve these local credit needs in a variety of ways. Each institution should be evaluated on the basis of its willingness to ascertain, and its determination to help meet, community credit needs in the context of its resources and local circumstances.

Balanced Viewpoint

The examiner should maintain a balanced perspective in conducting a CRA examination. The examiner cannot norinally conclude on the basis of any one factor that an institution is or is not helping to meet the credit needs of its local community or communities. Nor can the examiner adequately assess a lender's performance on the basis of any one source of information, data, or opinion. For that reason, the procedures contained in this section are designed to ensure that information from both the institution and the community are objectively reviewed and evaluated.

Institution's Input

The examination procedures give each institution the opportunity to supply information indicating that it is having a beneficial influence on its local community or communities. Institutions that are helping to meet community credit needs are proud of that fact and will be of substantial assistance to the examiner in assessing their performance.

Institution's Financial Condition and Size, and Legal Impediments and Local Economic Conditions

An institution's ability to help meet community credit needs is influenced by its financial condition and size as well as by legal impediments and local economic conditions under which it operates. An examiner must take these considerations into account in reviewing the institution's performance.

Technical Compliance with the Regulation

The examiner will check for technical compliance with the requirements of the regulation. However, compliance with procedural requirements does not imply that a lender has been serving local credit needs. The converse is also true; noncompliance with a technical requirement does not necessarily mean that an institution is not helping to meet community credit needs. The examiner must not lose sight of the intent of the statute in checking for technical compliance with the regulation. The entire CRA examination is designed primarily to determine the extent to which a lender has helped and is helping to meet community credit needs.

Communication, Community Development, and Low- and Moderate-Income Neighborhoods

In reviewing the record, the examiner should bear in mind the special emphasis placed by CRA on effective communication and community development activities. With respect to communication, the premise is that community needs which can be met on a safe and sound basis are more likely to be met when the community is aware of the types of credit available and the lender is well informed about community credit needs. Hence, efforts to ascertain community credit needs and to publicize available credit services, including measures to identify the credit needs of, and to advertise in, low- and moderate-income neighborhoods, are encouraged.

Outside Contacts

The examining staff should normally conduct interviews with community members to determine the local perception of community credit needs. Such members might include local development corporations, nonprofit housing development corporations, community development corporations, housing

counseling service centers, minority and non-English speaking groups, coalitions of neighborhood organizations, consumer, local civil rights, religious organizations, merchants associations, the PTA, and customers of the institution.

CRA also focuses on activities that foster development within the entire community, including low- and moderate-income neighborhoods. Consequently, housing related extensions, participation in community development programs and small business financing, including loans to small farms are viewed favorably.

Selected Features of CRA Examinations

CRA Statements

An institution must prepare a separate CRA Statement for each local community it serves, including a delineation of the relevant local community. It does not necessarily follow, however, that the CRA Statement prepared for each local community must contain a unique list of available credits. A lender serving several local communities may elect to prepare CRA Statements which contain lists of credits which are similar or identical for the local communities served. Since credit needs may be common to many local communities, such an approach may be consistent with the intent of CRA. There are other ways for a multi-community lender to satisfy this requirement. The examiner need not be especially concerned with the specific method employed by a multi-community institution so long as it makes a good-faith effort to inform members of each local community about their community's boundaries and the types of credit extended there.

Reasonableness of Community Delineation

Each institution must delineate the local community or communities which it serves. For instance, a statewide branching institution would serve a number of "local communities" the total of which would constitute its "entire community." Further, more than one office of an institution may serve the same local community. For example, an institution may have offices throughout a city and its suburbs and consider that entire metropolitan area to be the local community for those offices. Each community delineation must, of course, include the contiguous areas surrounding each office or group of offices.

Because many factors influence the size and shape of a lender's community, the regulation allows three acceptable methods of delineation and provides guidelines to assist each institution in defining its local community or communities.

The first method suggests the use of widely recognized existing boundaries such as those MSAs or counties for delimiting an institution's local community or communities. Such boundaries frequently constitute a reasonable approximation of the institution's local community.

In general, a local community based on existing boundaries should be no larger than an entire MSA or a county in a non-MSA area. If an institution has offices in more than one such area, it will have more than one local community. When an institution has an office near the boundary of the MSA or county, it should include those portions of adjacent counties that it serves. In rural areas, a local community may sometimes encompass more than one county, but, generally, institutions should not use states or regions of states to delineate local communities. A small institution that serves an area smaller than an MSA or county may define its community to be a part of the MSA or county. The institution may make adjustments in the community delineation in the case of areas divided by state borders, or significant geographic barriers, or areas that are extremely large or of unusual configuration.

The second method proposes the use of effective lending territory. Effective lending territory means that area around each office where the lender makes a substantial portion of its loans and all other areas equally distant. Even if an institution employs its effective lending territory, it is encouraged to follow existing boundaries where practical.

One should not conclude from this guideline that each office necessarily serves a separate and distinct local community because each office typically has a different, though possibly partially overlapping, effective lending territory. If an institution is represented throughout a trade or market area, it may be more reasonable to suppose that area comprises its local community.

Finally, the regulation allows an institution to use any other reasonably delineated area. An institution is thus given substantial leeway in specifying its local community so long as the definition is reasonable; that is to say, the institution can provide a sensible rationale for the delineation and has not arbitrarily excluded any low- and moderate-income neighborhoods.

Some Rules of Thumb on Reasonableness

The examiner should question the appropriateness of a sharply asymmetrical local community. That is not to say, however, that an irregularly shaped community cannot be justified.

Of course, the number and location of offices in an area influence the size of the institution's local community. For similar size institutions, those in rural areas tend to serve a larger geographic area (because of the lower population density) than those in urban areas.

Other factors which influence the shape of an institution's community include traffic patterns, natural and artificial barriers such as a river or an airport, legal boundaries such as state borders, and the institution's size.

If a question remains regarding the reasonableness of an institution's community delineation, the examiner may obtain CRA Statements from similar institutions in the local community and review their community delineations. Such a review may provide additional information valuable in judging the reasonableness of a lender's community delineation. Community groups can also provide information about the nature of an institution's delineation.

Low- and Moderate-Income Neighborhoods

In determining whether the community definition is reasonable, the examiner must be alert to situations where low- and moderate-income neighborhoods are gerrymandered out of a delineated area. Moreover, in reviewing an institution's record, the examiner must focus particular attention on the lender's performance in low- and moderate-income neighborhoods within a local community.

For neighborhoods located in MSAs, low- and moderate-income neighborhoods are defined by the FHLBB as follows: low-income neighborhoods consist of those census tracts which have median incomes which are less than or equal to 80 percent of the MSA median income; moderate-income neighborhoods are those which have median incomes of greater than 80 percent but less than or equal to 95 percent of the MSA median income.

Computer printouts identifying low- and moderate-income areas within MSAs are available to the District Banks for those institutions that are located in MSAs. The printouts are broken down into three groups, the first two groups represent the low-income and moderate-income census tracts as defined above. The third group consists of those census tracts which have median incomes greater than 95 percent of the MSA median income. The third group is available since the examiner may find that some census tracts have declined in median income since 1980 and thus, even though they did not qualify as low- or moderate-income in 1980, they do now. The examiner should consider this point in reviewing an institution's activities in low- and moderate-income areas.

The data columns appearing on the printouts are self-explanatory with the exception of the fifth column. This column is meant to indicate whether a particular census tract is "substantially minority" as defined in the instructions for preparation of the loan application register. "Substantially minority" census tracts are those in which the minority residents constitute 25 percent or more (either Black or Hispanic) of the total population in the census tract. This column can be used to check the information contained in the institution's loan application registers.

The examiner will note that many of the census tract printouts include the following footnote: "These census tracts included group quarters." Group quarters are defined by the U.S. Department of Commerce as follows: "Group quarters are living arrangements for institutional inmates or for other groups containing five or more persons not related to the person in charge. Group quarters are located most frequently in institutions, boarding houses, military barracks, college dormitories, fraternity and sorority houses, hospitals, monasteries, convents, and ships. A house or apartment is considered group quarters if it is shared by the person in charge and five or more persons unrelated to him, or if there is no person in charge, by six or more unrelated persons. Information on the housing characteristics of group quarters was not collected in the census." Housing characteristics columns on the data printouts are the following: Occupied Housing Units; Percentage Black Occupied, Percentage Black Owner; Percentage

Owner Occupied; Percentage Units Built 1939 or earlier; and 1-4 Family Structures. These columns do not include information on group quarters.

If a census tract has group quarters, it is flagged as having group quarters regardless of whether data were suppressed to avoid disclosing information on individuals. However, data suppression for the census tract, in such cases, may be indicated if the median income is shown as zero and/or the number of occupied housing units is less than 50.

The printouts do have certain limitations. Most of the data comes from the 1980 census and thus is rather old. Some census tracts may have radically changed since then. The examiner will have to rely on his or her own knowledge of the area, discussions with management, real estate brokers, city officials, and neighborhood groups, more recent local studies, property inspections, etc., in resolving any controversies over the current demographics of the census tracts.

Non-MSA areas, especially rural areas, present a particular problem in identifying low- and moderate income neighborhoods. Examiners have to rely on personal knowledge of the area, physical inspection as necessary, discussion with institution personnel, local studies, or a combination of these.

Small Business Lending

Small business loans represent one type of credit that is directly related to the purposes of CRA. In considereing small business lending, the examiner shouldnot be concerned with any hard and fast or precise definition of what constitutes a small business. Instead, the examiner should regard as small business lending any loans to local firms whose access to credit is limited to local sources because of the firm's size.

Examination Objectives

To determine whether the institution has established and implemented policies and procedures that deanonstrate:

- that it has recognized its continuing and affirmative obligation to help meet the credit needs of its entire community; and,
- that its facilities serve the credit conveniences and needs of its entire community.

To determine whether the institution's delineation of its community is in accordance with the regulatory requirements.

To determine the institution's compliance with statutory and regulatory requirements and policy statements.

Examination Procedures

1. Ascertain from institution personnel what steps the institution has taken or plans to take which indicate whether it is helping to serve the credit needs of its local community or communities.

2. Obtain the following:

a. minutes of the board of directors' meetings, particularly those dealing with the adoption, review, and revision of all CRA Statements.

b. the institution's public comment files and recent CRA Statements.

c. comment letters received by the Federal Home Loan Bank.

d. the institution's loan and investment policy and procedural manuals along with other manuals relating to the CRA.

3. Review minutes of directors' meetings and verify that the board has:

a. adopted a CRA Statement for each delineated community.

b. reviewed each statement at least annually.

c. acted upon any material change in each statement at the first regular meeting of the board following the change.

4. Review and analyze the public files for:

a. any signed written comments received from the public during the past two years that specifically relate to any CRA Statement or to the institution's performance in helping to meet the credit needs of its community or communities. Determine that the comments do not contain any material specifically prohibited by the regulation. However, the examiner shall consider letters containing any such material.

b. any responses to the commentors that the institution may have made.

c. all CRA Statements in effect during the past two years.

(Inherent in the process of reviewing public files is the option of contacting commentors to the extent deemed necessary.)

5. Review each CRA Statement in effect during the past two years and:

a. ascertain if the institution's delineation of its local community or communities is reasonable. Give special attention to the following:

- considerations used by the institution to define its community.
- community boundaries that are sharply asymmetrical, too narrowly drawn, or so broad that the institution fails to focus on its local community.
- whether any low- and moderate-income neighborhoods have been arbitrarily excluded.
- public comments specifically relating to the reasonableness of the institution's delineation.
- any relevant information obtained from other work programs that have been performed.

If a question remains regarding the reasonableness of the community delineation, a review of the community boundaries drawn by comparable local institutions may provide useful information.

b. review and analyze for completeness specific types of credits within certain categories that the institution is prepared to extend within the local community. Determine if the types of credit in the CRA Statement correspond to the types of credit actually being extended by the institution. Request explanations for any differences. If feasible and appropriate, review the list of available credits prepared by comparable local institutions.

c. determine that a copy of the CRA Public Notice is included.

d. analyze any of the following optional information that the institution may have included:

- a description of how its efforts, including special credit-related programs, help to meet community credit needs.
- a periodic report regarding its record of helping to meet community credit needs.
- a description of its efforts to ascertain the credit needs of its community, including efforts to communicate with members of its community regarding credit services.
- any other material the institution may have included.

6. Determine if the institution:

a. provides the CRA Public Notice in a manner specified by the regulation.

b. makes all CRA Statements available to the public as provided by the regulation.

c. makes the public comment files readily available for public inspection as provided in the regulation.

7. Review the institution's credit underwriting and appraisal criteria and terms and conditions of loans to determine if they are being used for exclusionary purposes, contrary to the objectives of CRA.

8. The institution's activities in determining credit needs and in helping to meet the credit needs of its community.

a. Activities conducted by the institution to ascertain the credit needs of its community, including the extent of the institution's efforts to communicate with members of its community regarding the credit services being provided by the institution.

Ascertain from records and through interviewing management and a sampling of community leaders and interest groups the extent to which the institution has communicated with members of its local community or otherwise has attempted to determine such need. Pertinent factors may include:

(1) management review of written, signed public comments received in response to the institution's CRA Statements.

(2) studies conducted or reviewed by the institution concerning local credit needs.

(3) the extent of the institution's efforts to communicate with members of its community regarding the credit services it is or could be providing. Such members might include customers of the institution, the PTA, merchants associations, religious organizations, coalitions of neighborhood associations, local civil rights, consumer, minority, and non-English speaking groups, housing counseling service centers, community development corporations, and nonprofit housing development corporations.

(4) the institution's review of the local government's Community Development Plan and Housing Assistance Plan prepared in conjunction with HUD's Community Development Block Grant Program.

(5) economic forecasting, as developed or used by the institution.

b. The extent of the institution's marketing and special credit-related programs to make members of the community aware of the credit services offered by the institution.

Review the institution's marketing and determine if it is adequately designed to encourage applications for loans in its community, particularly low- and moderate-income neighborhoods. Pertinent factors may include:

(1) any working relationships the institution may have with real estate brokers or others who service low- and moderate-income neighborhoods.

(2) mortgage counseling programs and programs of management assistance for small or minority businesses.

(3) development and participation in mortgage review boards.

(4) credit and credit-related services in low- and moderate-income neighborhoods compared to such services in other neighborhoods served by the institution.

(5) use of institution representatives for seeking out potential housing-related and small business demand in low- and moderate-income neighborhoods.

(6) advertising the types of loans the institution is willing to make in media likely to reach low- and moderate-income individuals in the institution's local community or communities.

(7) availability of convenient hours in offices accessible to residents of low- and moderate-income neighborhoods.

(8) use of informational brochures and participation in other educational efforts.

c. The extent of participation by the institution's board of directors in formulating the institution's policies and reviewing its performance with respect to the purpose of the CRA.

d. Any practices intended to discourage applications for types of credit set forth in the institution's CRA Statement.

Review other nondiscrimination examination programs, particularly as they pertain to interviewing and prescreening. Additionally, ascertain the following:

(1) whether administrative loan personnel and loan officers are aware of the CRA and the requirements of the regulation.

(2) whether lending officers are aware of the institution's delineation of its local community or communities and its policies, if any, with respect to its commitment to help meet the credit needs of its entire community, including low- and moderate-income neighborhoods.

(3) whether loan officers are aware of the types of credit the institution offers to members of its local community or communities.

(4) whether public contact personnel are aware of the availability of the institution's CRA Statement and public comment file.

(5) whether the institution is prepared to extend types of credit in some local communities or neighborhoods but not in others. An explanation of any difference should be requested from the institution.

(6) the extent to which the institution is willing to make loans in its delineated local community or communities, utilizing information derived in (e.) below. Special attention should be given to specific reasons why loan applications have been denied, whether or not such denial has been on a prohibited basis.

(7) whether loan officers or other public contact personnel prescreen potential applicants from obtaining loans that the institution has stated it is willing to make, particularly applicants from low- and moderate-income neighborhoods.

e. The geographic distribution of the institution's credit extensions, credit applications, and credit denials.

Determine whether there is any indication of a geographic distribution of credit extensions, applications for credit, and credit denials which would signify failure to serve selected areas of local communities, particularly low- and moderate-income neighborhoods. Initial reliance may be placed upon discussion with other examiners, review of reports of examination, and review of work papers from other programs performed. For those institutions located in MSAs, additional reliance may be placed upon other nondiscrimination examination programs for ascertaining the volume and location of housing-related credits.

For loans made outside MSAs, particularly with respect to institutions that are not located in such areas, interview management and review internal files to determine the extent of housing-related lending in low- and moderate-income neighborhoods and the extent to which the institution has not extended such credit in those areas.

Reliance may be placed on geocoding of credit extensions, credit applications, and credit denials. The examiner will review the loan application registers to determine the geographic distribution of loans, applications and denials. In conjunction with other nondiscrimination examination programs, it may be necessary to analyze further the geographic distribution of small business loans, including loans to small farms within the institution's local community.

f. Evidence of prohibited discriminatory or other illegal credit practices.

In connection with the nondiscrimination examination programs, determine the extent to which the institution is currently complying with the law.

g. The institution's record of opening and closing offices and providing services at offices.

Information can be provided by the District Bank or obtained from the institution's records. Ascertain the impact of such activities through the interviewing process and the review of public comments with particular focus on low- and moderate-income neighborhoods.

h. The institution's participation , including investments, in local community development and redevelopment projects or programs.

Review written lending policy and procedural manuals and interview lending officers to ascertain whether current programs include, or if the institution has considered involvement in, programs for satisfying potential credit needs such as the following:

- Community Investment Fund
- HUD's Community Development Block Grant Program.

- Local neighborhood preservation efforts.
- Community Development Corporations.
- Financing for Local Development Corporations.
- Neighborhood Housing Services.
- Investments in, or coordination with, Minority Enterprise Small Business Investment Corporations (MESBICs) or Small Business Investment Corporations (SBICs) in providing loans to business for which equity or subordinated debt is provided by MESBIC or SBIC.
- Purchase of securities of State and local housing agencies.

i. The institution's origination of residential mortgage loans, housing rehabilitation loans, home improvement loans, and small business or small farm loans within its community, or the purchase of such loans originated in its community.

Review the institution's financial statements, other appropriate records including HMDA Statements, its written lending policy and procedural manuals, and interview lending personnel to ascertain whether the institution has originated or purchased such loans or has plans to do so.

j. The institution's participation in governmentally-insured, guaranteed, or subsidized loan programs for housing, small business or small farms.

This information may be obtained in ways similar to the ones in assessment factor (i) above. Examples of such government loan programs include:

- FHA/VA/FMHA mortgage loans to members of its community or communities.
- FHA Title I home improvement loans.
- SBA loan guaranty programs.
- Similar programs conducted by State or local agencies.

k. The institution's ability to meet various community credit needs based on its financial condition and size, and legal impediments, local economic conditions, and other factors.

The financial condition of the institution may be ascertained from discussion with other examiners or review of examination work papers and reports.

Small institutions may not have the specified staff or financial resources needed to participate in some loan programs. Legal restrictions on permissible activities, interest rates, and branches may affect a lender's ability to help meet community credit needs. Adverse economic conditions caused by local or general economic difficulties may force an institution to temporarily curtail its lending activities. Other factors may affect an institution's ability to help meet community credit needs.

l. Other factors that in the agency's judgment reasonably bear upon the extent to which the institution is helping to meet the credit needs of its entire community.

Pertinent factors may include:

- purchases of state and municipal bonds, secondary mortgage market securities or such other activities when they further special purposes in the community, such as the construction or rehabilitation of low- and moderate-income housing or other neighborhood or community development, or are issued by municipalities or other local public financing units which do not have access to the capital markets.
- whether the institution's policies promote efforts to assist existing residents in neighborhoods undergoing a process of reinvestment and change.
- any other relevant factors.

9. Determine if the record of performance of the institution's facilities demonstrates its recognition of its continuing and affirmative obligation to help meet the credit needs of its entire community including low- and moderate-income neighborhoods, consistent with safe and sound operation.

10. Complete the CRA Checklist (CA 220).

11. Review the following with management:

a. the extent to which the institution is helping to meet the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with safe and sound operation.

b. suggestions that might better enable the institution to help meet the credit needs of its entire community and improve its CRA rating.

c. procedural violations of the regulations.

d. deficiencies or exceptions in policies or practices.

12. Prepare a narrative statement for the examination report (see Section 110-1).

13. Assign a rating of 1 to 5 based on the institution's overall CRA performance (see Section 110-2).

References

Regulations

12 CFR 563e	Federal Home Loan Bank Board Regulations

(See also Nondiscrimination—General, Section 200.)

Community Reinvestment Act
Checklist

	Yes	No
1. Has the Board of Directors adopted its CRA Statement? (§ 563e.4(a))		
2. Is the CRA Statement clear and concise?		
3. Have all changes in the Statement been approved by the Board of Directors at its first regular meeting following the change? (§ 563e.4(d))		
4. Do the minutes indicate annual review of each Statement? (§ 563e.4(d))		
5. Does the Statement contain:		
a. A delineation of the institution's entire community including local communities, if any? (§ 563e.4(b)(1))		
b. A list of the types of credit the institution is prepared to extend to its entire community? (§ 563e.4(b)(2))		
c. The required notice either as a part of the Statement or as an attachment? (§ 563e.4(b)(3))		
6. Is a notice provided in the public lobby of institution offices either as a part of the CRA Statement or separately? (§ 563e.6)		
7. Is the notice in the form provided by the Regulation? (§ 563e.6)		
8. Are the CRA Statements readily available at the head office and at each office of the institution in the local community? (§ 563e.4(e)(1) and (2))		
9. If a charge is made for the CRA Statement, do records indicate this charge does not exceed cost of reproduction? (§ 563e.4(f))		
10. Does the institution maintain a "public file" as required? (for the two most recent years) (§ 563e.5)		
11. Is the location of public files in accordance with the Regulation? (§ 563e.5(c) (1) and (2))		
12. Are public files readily available for public inspection? (§ 563e.5(a))		
13. Were the considerations used by the institution to define its community reasonable? (§ 563e.3)		
14. Were all comments on community definition in the public file considered by the institution?		
15. Does the lender's delineation of community include all low- and moderate-income neighborhoods? (§ 563e.3(a))		
16. Are the delineated areas reasonable?		
17. Were all comments in the public file relative to types of credit considered by the institution?		
18. Are the kinds of loans made by the institution comparable to the types of credit offered in the CRA Statement?		
19. Are all lending personnel informed of the types of credit the institution is prepared to extend?		
20. Does the CRA Statement describe how the institution's efforts, including special programs, help meet the credit needs of the community? (§ 563e.4(c)(1))*		
21. Does the CRA Statement include a report of the results of its efforts to help meet local credit needs? (§ 563e.4(c)(2))*		
22. Does the CRA Statement include a description of its efforts to ascertain community credit needs and communicate with members of its community? (§ 563e.4(c)(3))*		
23. Did the institution review the CRA Statement in light of community comments and its experience in offering various kinds of credit?		

*Note: These items are not required to be included in the CRA Statements. Such inclusion is only encouraged by the Regulation.

Reviewed
By Date

Community Reinvestment Act
Checklist

	Yes	No
24. Does the institution consult with members of its local community about its plans and policies on available credit services?		
25. Does the institution invest in the following types of loans originated within its communities: (§ 563e.7(i))		
a. Residential mortgage?;		
b. Housing rehabilitation?;		
c. Home improvement/equipping?;		
d. Small business?;		
e. Small farm?.		

Comments _____

Reviewed
By Date

EXHIBIT F

Average CRA Hours Per Examination
By Asset Size Ranges
1983 - 1988

Year	< $25M Avg. Hrs.	$25-100 Avg. Hrs.	$100-500 Avg. Hrs.	$500+ Avg. Hrs.	Total Avg. Hrs.
1983	3.66	4.82	6.83	11.46	5.87
1984	3.09	3.91	6.62	9.87	5.46
1985	2.91	4.57	6.47	11.22	5.82
1986	4.17	5.88	9.40	17.03	8.20
1987	3.57	5.20	7.12	23.72	7.92
1988	4.84	6.24	9.12	21.25	8.89
Total	3.75	5.21	7.67	16.83	7.19

NOTE: Asset size ranges are in millions of dollars

EXHIBIT G

Federal Home Loan Bank Board

1700 G Street, N.W.
Washington, D.C. 20552

Federal Home Loan Bank System
Federal Home Loan Mortgage Corporation
Federal Savings and Loan Insurance Corporation

July 17, 1989

The Honorable Henry B. Gonzalez
Chairman
Committee on Banking, Finance
and Urban Affairs
House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

We are confirming our support for the amendments to the House Bill (H.R. 1278) improving oversight and enforcement of the fair lending and community reinvestment laws. These include "Sec. 1211. Fair Lending Oversight", "Sec. 1212. Amendment To The Community Reinvestment Act", and "Sec. 1213. Reports On Geographic Origin Of Deposits Of Depository Institutions". These amendments are appropriate supplements to equal housing lending programs, community investment initiatives, and fair housing enforcement.

The thrift industry and the Bank Board have been in the forefront of efforts to collect data for use in advancing equal housing lending, promoting community investment, and enforcing nondiscrimination laws and regulations. Our data collection and reporting systems (such as the Loan Application Register and Data Submission Reports) are unique among the federal financial regulatory agencies. With the establishment of our new consumer compliance division with a specialized examination force, we are making more effective use of the data collected.

The next logical step in data collection, reporting, and analysis relating to equal housing lending is to make such requirements mandatory for all lenders. Such an expansion will improve our knowledge and allow targeting of programs to meet individual and community credit needs.

Section 1211 would amend the Home Mortgage Disclosure Act to require reporting by all mortgage lenders as opposed to the current coverage of only depository institutions and holding company subsidiaries. It would also require the reporting of income levels of borrowers, racial characteristics, and gender. We fully support both of these objectives. This amendment will cause only a minor increase in the reporting burden of our institutions, because the Bank Board already collects most of the information under the Loan Application Register and Data Submission Report requirements of 12 C.F.R Part 528 of our regulations. Requiring reporting by all mortgage lenders will benefit fair housing enforcement, community investment promotion, and competitive equality among all lenders.

We do suggest that some provision be made for the monitoring of reporting by newly-covered mortgage lenders. A federal agency should be assigned clear authority to monitor and enforce the reporting requirements of lenders not currently regulated by a federal financial regulatory agency.

Section 1212 would amend the Community Reinvestment Act ("CRA") to require the federal financial regulatory agencies to publish detailed CRA evaluations of institutions upon the completion of CRA examinations and to release the institution's CRA rating. We support the thrust of this change, but we are concerned that the CRA numerical rating could be confused with an institution's financial numerical rating. Therefore, we propose that CRA rating system be changed from a numerical one to a descriptive one and the descriptive rating disclosed. For example, the rating system could include "Good", "Satisfactory", and "Unsatisfactory" or some other set of terms that would clearly rate performance, but not risk confusion with financial soundness ratings.

Section 1213 would require the Federal Reserve Board to collect data and conduct studies on the geographic origins of deposits. This information could help in better understanding the complexities of our changing financial markets and in the better formulation of financial policy.

At the same time, we urge the Congress to recognize the financial markets are constantly becoming more national, and even international, in scope and that regulatory efforts to confine financial institutions to serving only limited, localized geographic areas can make these institutions more vulnerable to fluctuations in local economic fortunes. Such efforts are thereby in conflict with the important goal of promoting the safety and soundness of these institutions. What is needed is a balanced approach--one that avoids allowing lenders to diversify carelessly into new product lines or geographic areas, thereby endangering safety and soundness and ignoring local customers, but also one that avoids confining these lenders to uneconomic activities or insufficient diversification.

Sincerely,

M. Danny Wall
Chairman

Lawrence J. White
Board Member

Senator DIXON. Thank you, sir.
Mr. McDowell.

STATEMENT OF JOHN H. McDOWELL, DIRECTOR OF CONSUMER ACTIVITIES, OFFICE OF THE COMPTROLLER OF THE CURRENCY, WASHINGTON, DC

Mr. McDOWELL. Mr. Chairman, I am pleased to have this opportunity to respond to the questions posed in your July 6, 1989 letter regarding our efforts under the Community Reinvestment Act.

I am Director of the Consumer Activities Division of the Office of the Comptroller of the Currency. My division has primary responsibility in the OCC for the administration of the examination procedures relating to consumer protection laws affecting national banks, including the CRA.

The OCC supports the objective of the CRA and oversees bank performance through a program that encourages positive action by the national banks. Cooperation among the OCC, the banks, and the banking public is essential for this effort.

My written statement focuses on the supervisory process employed by the OCC to fulfill its responsibilities under the CRA. The first section describes how our supervisory efforts for CRA are integrated into our overall approach to bank supervision.

The next section provides a more detailed analysis of our examinations and our efforts to maintain an ongoing dialogue with bank customer and community groups and with national banks.

The final section of this testimony outlines our views regarding the appropriate disclosure of information to the public and the level of public participation in our CRA.

In the interest of time, Mr. Chairman, I will limit my oral testimony to a brief discussion of the OCC's CRA efforts.

Compliance with the CRA is assessed through consideration of a number of both positive and negative factors. They include activities conducted by the bank to ascertain community credit needs, the extent of the bank's marketing efforts to make community members aware of credit services, participation by the bank's board of directors in formulating the bank's policies and reviewing its CRA performance, the existence of practices intended to discourage application for credit from the local community, geographic distribution of the bank's credit extensions, applications and denials, evidence of prohibited discriminatory practices, the bank's record of opening and closing offices, participation in local development projects, and the bank's origination of loans for residential mortgages, home improvement, housing rehabilitation, and small businesses or small farms.

Examiners assess a bank's CRA performance by reviewing its CRA statement, ensuring the accuracy and completeness of products and services offered, and reviewing whether the community delineated by the bank is either too narrowly or broadly drawn. In discussions with line officers and management assigned to coordinate CRA activities and by reviewing the bank's documented evidence, the examiners determine the bank's efforts to ascertain the credit needs of its entire community.

The examiners then review the bank's loan policies and credit approval standards to ensure that, considering its resources and financial condition, it is helping to meet those needs.

Board minutes are also reviewed to be sure that the directors are informed of the bank's CRA-related activities, are active in formulating appropriate CRA-related policies, participate in the monitoring of the bank's performance, and that they not only review but approve the CRA statement.

As appropriate, the examiners also conduct meetings with local community groups to determine what their perceptions are of the community's credit needs and whether national banks in the community are helping to meet those needs.

The OCC uses the uniform interagency rating system for evaluating the performance of federally regulated institutions under the CRA. A rating is assigned to each financial institution based on the institution's performance in meeting community credit needs. This rating is based on a subjective analysis of the bank's performance and is but a general indicator of the bank's overall CRA assessment.

BANK RATINGS

Banks may be given CRA ratings ranging from 1 to 5. The top rating a bank can receive is 1. A rating of 3 is given to banks whose CRA performance is less than satisfactory. A 5 rating represents a substantially inadequate record of helping to meet community credit needs.

We do not believe that a large number of banks should necessarily fall into the 3, 4, and 5 rating categories. In general, banks have found that it is in their best interest to serve their community. Therefore, they historically have worked hard to meet local community credit needs consistent with safety and soundness requirements, and we have found that they continue to do so.

An integral part of the examination is the report provided to bank directors and management summarizing the results of the examination. The report normally contains the examiner's assessment of the bank's CRA performance and recommendations for improving that performance. These recommendations to enhance or improve performance are also discussed with management and the board of directors at the conclusion of the examination. This guidance helps promote a high level of CRA performance.

The examination report is also the key document used by the OCC in monitoring CRA performance. Field examiners use the report to review performance and prepare for subsequent examinations. District personnel use the report to ensure thorough supervision of examined banks and to develop supervisory strategies. Corporate analysts in the districts and in Washington use the report in evaluating corporate applications.

Disclosure of CRA numeric ratings also has been proposed. The OCC recognizes that disclosure of a bank's performance would serve to increase the public's awareness. In light of the recent conference committee decision to amend the CRA to include disclosure of assigned ratings and written evaluations of the institution's per-

formance, the OCC will of course make the necessary adjustments to comply with the act.

In summary, the purpose of CRA is to encourage financial institutions to assess and help meet the credit needs of their communities, including low and moderate income neighborhoods, utilizing their own expertise and resources. The OCC believes it has implemented appropriate systems for assessing the level of performance under the CRA, encouraged improvements to national banks' performance through examinations, education, outreach, and communications activities, and enforced the spirit of the statute through the corporate application process.

We recognize that there is always room for improvement, and we welcome recommendations that the subcommittee has to offer.

Thank you, Mr. Chairman and members of the subcommittee, for this opportunity to present OCC's views on this important subject.

[The complete prepared statement of John H. McDowell follows:]

For Release:
July 31, 1989, 2:00 p.m.

TESTIMONY OF
JOHN H. McDOWELL, DIRECTOR
CONSUMER ACTIVITIES DIVISION
OFFICE OF THE COMPTROLLER OF THE CURRENCY
Before the
SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS
of the
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE
July 31, 1989

Introduction

Mr. Chairman, I am here today to discuss the Office of the Comptroller of the Currency's (OCC) efforts under the Community Reinvestment Act (CRA) and to respond to the specific questions posed in your July 6, 1989 letter. The OCC supports the objectives of the CRA and oversees bank performance through a program that encourages positive action by the national banks. Cooperation among the OCC, the banks, and the banking public is essential to this effort.

My testimony today will focus on the supervisory process employed by the OCC to fulfill its responsibilities under the CRA. The first section describes how our supervisory efforts for CRA are integrated into our overall approach to bank supervision. The next section provides a more detailed analysis of our examinations and our efforts to maintain an ongoing dialogue with bank customer and community groups and with national banks. The final section of this testimony outlines our views regarding the appropriate disclosure of information to the public and the level of public participation under CRA.

OCC's Supervision for CRA

The OCC's responsibilities under CRA are discharged in accordance with our overall supervisory philosophy. First and foremost, a bank's performance is the responsibility of its board of directors and management. Banks must establish policies and procedures consistent with the spirit and intent of the CRA and systems of control to ensure that those policies and procedures are effectively

implemented. During examinations, we monitor whether the banks' systems work, and we require changes when necessary. Our dual strategy of requiring systems for bank compliance with the law and monitoring the performance of those systems underlies our supervisory process, not only with regard to the CRA, but with regard to all assessments of bank compliance.

The Compliance Program

Since early 1987, the OCC has assessed a bank's performance under CRA as one facet of its review of compliance with a number of laws and regulations. The Compliance Program includes procedures for determining adherence to the Bank Secrecy Act, fair lending laws, such as the Equal Credit Opportunity and the Fair Housing Acts, insider and affiliate transactions, consumer protection laws, such as the Truth in Lending Act, and adherence to fiduciary principles in the performance of fiduciary duties as well as compliance for CRA. The operation of electronic data processing centers and bank dealer activities are also examined.

Each year, we select a statistically valid random sample of national banks with assets of less than $1 billion for an in-depth review of their compliance efforts and accomplishments. National banks with assets in excess of $1 billion are examined every other year. Although we do not examine every bank every year for compliance, we believe the sample size is sufficiently large to allow us to determine whether national banks are, in general, meeting their CRA responsibilities. Those banks that we do not examine in a particular year have an incentive to comply with the law because of the uncertainty associated with being selected in the sample.

In addition to the CRA assessments conducted in the sample of banks, other CRA assessments are conducted through targeting and special investigations. Banks may be targeted for CRA examinations if they are known to be planning an expansion through merger or branching, if unsatisfactory operating procedures are discovered through the commercial examination, or if the supervising examiner determines that the previous CRA assessment is outdated. Later in my statement, I will describe in some detail our specific examination efforts regarding CRA.

The OCC does not rely solely on examinations to encourage banks to meet their CRA obligations. We also make sure, through the use of banking issuances and advisories, that bank management is aware of its compliance responsibilities. Advisories and banking bulletins, covering a broad spectrum of issues including speculative trading activities, disclosure of the method of calculating interest on deposit accounts, banks' investments in government securities mutual funds, home equity lines of credit, discounted variable rate mortgages, the Flood Disaster Protection Act, and the CRA Policy Statement (discussed in more detail later in this testimony) have been distributed to the industry.

Our efforts also include OCC participation in formal industry education programs. In 1987 and 1988, the OCC, through its Consumer Activities Division, provided speakers for over 60 seminars and training sessions sponsored by trade and state banking associations and for individual banks promoting compliance with consumer protection laws and regulations. The OCC maintains an ongoing program of activities to facilitate increased banking industry sensitivity to customer and community needs. These activities, carried out principally through the Customer and Industry Affairs Division, are designed to:

- Identify and assess key issues and concerns raised by bank customer groups and communicate these concerns to national banks;
- Provide information to banks through conferences, roundtables and publications highlighting a variety of positive approaches and program models banks can and do use to help meet special credit needs in their communities and fulfill their CRA responsibilities; and
- Promote the use of bank community development corporations and community development investments as one tool to help banks meet community credit needs.

Additional information concerning the OCC's educational and communications activities which supplement the CRA examination and corporate application processes is attached as Appendix 1 to this testimony.

Another aspect of the Compliance Program consists of efforts to simplify compliance with regulations. For example, we developed a microcomputer program that makes it much easier to compute accurate annual percentage rates, in conformity with Federal Reserve Regulation Z. This program was distributed to all OCC examining staff, the FDIC, the Federal Reserve Board, the Federal Home Loan Bank System, and various state banking regulators. It is also made available to the banking industry through the OCC and the American Bankers Association.

After the completion of the first cycle of compliance examinations in April, 1988, we analyzed the extensive examination data collected from the banks examined. The most important objective of the analysis was to develop information to improve industry compliance. Our analysis showed that, in general, financial performance and size of the bank are unrelated to compliance performance. The results of this analysis will enable us to develop more effective supervisory tools.

Finally, when we detect violations, we take appropriate action to require correction of detected problems. For the time period beginning with the inception of the Compliance Program through year-end 1988, 17 enforcement actions were taken against national banks solely on the basis of identified compliance problems. Another

208 enforcement actions were taken partially on the basis of compliance problems. By strictly requiring corrective action for detected problems, we are deterring noncompliance.

I will now turn to the OCC's examination efforts to specifically address the CRA performance of national banks.

The OCC's CRA Efforts

CRA Examinations

Compliance with the CRA is assessed through consideration of a number of both positive and negative factors. They include: activities conducted by the bank to ascertain community credit needs; the extent of the bank's marketing efforts to make community members aware of credit services; participation by the bank's board of directors in formulating the bank's policies and reviewing its CRA performance; the existence of practices intended to discourage applications for credit from the local community; geographic distribution of the bank's credit extensions, applications, and denials; evidence of prohibited discriminatory practices; the bank's record of opening and closing offices; participation in local development projects; and the bank's origination of loans for residential mortgages, home improvement, housing rehabilitation, and small businesses or small farms.

Examiners assess a bank's CRA performance by reviewing its CRA Statement, ensuring the accuracy and completeness of products and services offered, and reviewing whether the community delineated by the bank is either too narrowly or broadly drawn. In discussions with line officers and management assigned to coordinate CRA related activities, and by reviewing the bank's documented evidence, examiners determine the bank's efforts to ascertain the credit needs of its entire community. The examiners then review the bank's loan policies and credit approval standards to ensure that, considering its resources and financial condition, it is helping to meet those needs and that such policies and procedures do not have an adverse effect on any consumer. Board minutes are also reviewed to ensure that the directors are informed of the bank's CRA-related activities, are active in formulating appropriate CRA-related policies, participate in monitoring the bank's performance, and that the CRA Statement is annually reviewed and approved. As appropriate, examiners also conduct meetings with local community groups to determine what are their perceptions of the community's credit needs and whether national banks in the community are helping to meet those needs.

Attached, as Appendix 2 to this testimony, is a table showing the twelve assessment factors used by national bank examiners in evaluating a bank's performance under the CRA and general examination procedures used for each factor.

Examination Results: CRA Ratings

The OCC uses the uniform interagency rating system for evaluating the performance of federally regulated institutions under the CRA. A rating is assigned to each financial institution based on the institution's performance in meeting community credit needs. This rating is based on a subjective analysis of the bank's performance and is but a general indicator of the bank's overall CRA assessment. Areas of evaluation include bank performance under the assessment factors detailed in the CRA regulation, comments from the community contained in the public files concerning bank performance under the CRA, and community contacts initiated by our office or by community groups. Banks may be given CRA ratings ranging from 1 to 5. The top rating a bank can receive is 1; a rating of 3 is given to banks whose CRA performance is less than satisfactory; a 5 rating represents a substantially inadequate record of helping to meet community credit needs. Appendix 3 to this testimony is a description of the Uniform Interagency CRA Rating System and the five performance categories identified within the rating system.

We do not believe that a large number of banks should necessarily fall into the 3, 4, and 5 rating categories. In general, we have found that banks historically have worked hard to meet local community credit needs, consistent with safety and soundness requirements, and that they continue to do so. However, we also note that increased training and sensitivity to CRA in recent years have improved our examiners' ability to evaluate bank CRA performance. This may account for the more critical ratings that we have recently experienced.

Following is a table that shows the distribution of ratings for the examinations conducted each year by OCC's district offices. The chart covers 1985 through June 30, 1989.

CRA Ratings By District

	Ratings	1	2	3	4	5
(1985)	Northeastern	27	36	1	0	0
	Southeastern	40	126	2	0	0
	Central	116	337	0	0	0
	Midwestern	61	253	3	1	0
	Southwestern	50	470	8	2	0
	Western	22	177	4	0	0
	Totals	316	1399	19	3	0
(1986)	Northeastern	56	247	6	0	0
	Southeastern	65	329	5	1	0
	Central	180	552	6	0	0
	Midwestern	118	599	7	0	1
	Southwestern	89	921	13	1	0
	Western	52	468	7	0	0
	Totals	560	3116	44	2	1
(1987)	Northeastern	23	138	7	0	0
	Southeastern	25	181	11	0	0
	Central	134	551	12	0	0
	Midwestern	56	421	4	0	0
	Southwestern	34	469	23	1	0
	Western	11	176	5	1	0
	Totals	283	1806	62	2	0
(1988)	Northeastern	11	99	10	1	0
	Southeastern	8	118	22	2	0
	Central	60	328	11	1	0
	Midwestern	10	172	10	0	0
	Southwestern	3	160	33	1	0
	Western	12	128	9	0	0
	Totals	104	1005	95	5	0
(1/89-6/89)	Northeastern	2	38	7	0	0
	Southeastern	5	36	5	1	0
	Central	19	134	5	0	0
	Midwestern	2	60	2	0	0
	Southwestern	3	77	16	2	0
	Western	1	50	6	0	0
	Totals	32	395	41	3	0

Examination Results: Reports to Bank Management

An integral part of the examination is the report provided to bank directors and management summarizing the results of the examination. The report normally contains the examiner's assessment of the bank's CRA performance and recommendations for improving that performance. These recommendations to enhance or improve performance are also discussed with management and the board of directors at the conclusion of the examination. This guidance helps promote a high level of CRA performance.

The examination report is also the key document used by the OCC in monitoring CRA performance. Field examiners use the report to review performance and prepare for subsequent examinations. District personnel use the report to ensure thorough supervision of examined banks and to develop supervisory strategies. Corporate analysts in the districts and Washington use the report in evaluating corporate applications.

Examination Time Devoted to CRA

In your letter of invitation, Mr. Chairman, you asked for information on CRA examinations, examination time, and examiner training. I noted previously that CRA performance is assessed by examiners during all compliance examinations that we conduct and during targeted CRA examinations. The OCC does not have precise information on the amount of time devoted specifically to on-site CRA examinations. However, we estimate that approximately 20 percent of the time spent on the consumer protection portion of an on-site compliance examination is devoted to CRA. Based on this estimate, we have calculated the amount of time the OCC has spent examining for compliance with CRA. Those calculations are presented in the following table.

Workdays Devoted to CRA Examinations by Bank

Asset Size	Work Days Per Bank Examined 1987	1988
Under $50 million	2.5	2.0
$ 50 million to $100 million	2.5	2.7
$100 million to $300 million	3.0	3.4
$300 million to $1 billion	4.5	5.6
$1 billion to $10 billion	9.0	8.1
Over $10 billion	16.5	21.0

Examiner Training

Examiners are trained to assess CRA as part of their broader compliance examination training. This training typically occurs after the examiner has been with the OCC between 12 and 30 months.

All examiners are required to take a compliance self-study course and a 40-hour tutorial on consumer protection laws produced by the OCC in cooperation with a banking trade association. Additionally, an eight-day consumer school is required for all examiners.

An advanced consumer compliance seminar is also offered to commissioned national bank examiners who have completed the district-sponsored consumer school and who conduct the consumer portion of compliance examinations. At the seminar, leaders from national banks, consumer and community groups, and other financial regulatory agencies offer different perspectives on a variety of consumer-oriented issues, including CRA. The OCC also offers a seminar, which includes CRA training, for managers who administer the compliance examination process in the field and who review compliance examination reports.

The following table reflects the number of examiners who have received consumer training, including CRA, from 1986 through year-end 1988. The majority of figures in the chart reflect examiners who were hired since 1985. Many other examiners received consumer/CRA training prior to 1986.

District	No. of Field Examiners	No. of Examiners Trained
Southeastern	239	122
Western	273	124
Midwestern	308	194
Northeastern	313	202
Southwestern	501	249
Central	353	197

Encouraging CRA Performance through the Application Process

The CRA does not give the OCC or any other financial regulatory agency the authority to initiate administrative enforcement action when a bank's CRA performance is less than satisfactory. Enforcement of the CRA is primarily through the corporate application process.

The OCC considers the CRA performance of national banks when evaluating their corporate applications for charters, charter conversions, branches, mergers, and relocations of home and branch offices. This information is derived from examinations conducted in the course of the Compliance Program, from targeted examinations or special investigations triggered by a corporate application, from data collected under the Home Mortgage Disclosure Act, and from public comments.

OCC policies and procedures for the disposition of corporate applications offer extensive opportunities for public comment. Those opportunities may be found in certain provisions of our regulation: 12 CFR Part 5, "Rules, policies, and procedures for corporate activities."

In particular, section 5.8 of that regulation requires an applicant to notify the public of its application by publishing a notice in a "... newspaper of general circulation in the community in which the applicant proposes to engage in business. The notice shall state that an application is being filed as of the date of notice, and the notice shall contain the name of the applicant(s) and the subject matter of the application." In addition to the requirement for public notice by the applicant, the OCC publishes a notification of receipt and disposition of applications in its Weekly Bulletin.

Section 5.9 requires the OCC to maintain a public file for each application. The public file contains the application and, with certain exceptions, supporting data and supplemental information filed by the applicant(s). It also contains "... all data and information submitted by interested persons in favor of or in opposition to such application...." Ordinarily, interested persons are given 30 days after the publication of the notice to provide comment. However, the OCC may extend the comment period if there are extenuating circumstances.

In accordance with the OCC's goal of processing corporate applications in a timely manner, extensions of the public comment period are rare. Extensions may be granted if the applicant failed to properly publish the notice of the application, or if the group desiring to protest is not located in the area where the applicant is required to publish, e.g., a group may want to protest a bank with statewide operations, but may not see the notice of a branch application filed in another area of the state. Extensions are granted for a limited period of time, normally to allow the protester the standard comment period from the date they actually received notice of the application or from the date notice was published in the Weekly Bulletin. We believe, however, that concerned groups need not and should not wait to communicate their concerns or problems until a bank has filed a corporate application.

When applications are protested on CRA grounds, the OCC encourages, but does not require, further communication between the contesting parties. Any agreement they might reach is not subject to OCC approval or enforcement. However, during subsequent CRA examinations, the OCC may find evidence that a bank has undertaken activities based on an agreement. These activities would be considered as part of the OCC's normal review of the bank's CRA record and could be a factor in the assessment and rating. In assessing the bank's overall CRA performance, we also take into account any effects that may result from a bank's decision not to meet with community groups.

An institution's CRA assessment is measured by its past performance in helping to meet its delineated community's credit needs. In general, commitments made during the application process cannot be used to overcome a seriously deficient record of CRA performance.

The OCC has approved applications with specific conditions requiring the applicant banks to strengthen their CRA performance. Under such circumstances, the banks cannot consummate the transactions in question until they provide concrete evidence to the OCC that their CRA performance has been strengthened. As a result, the conditional approval approach provides the OCC with substantial enforcement leverage by explicitly tying improvement of a bank's CRA performance to its achievement of a desired objective. This procedure produces results, and communities benefit through the improvements made in response to the OCC-imposed conditions. If, on the other hand, the application was simply denied, the bank may not implement CRA performance improvements and the community would experience no benefit from the denial.

In addition to the OCC's action on the approval of applications, the objectives of the CRA can be promoted by meetings between applicants and concerned community groups while an application is in process. However, the OCC does not require or intervene in such meetings. We do not have the authority to approve any agreements that may be negotiated between applicants and community groups.

Following are tables reflecting the number and disposition of protested applications and the number of all CRA related applications.

Community Reinvestment Act Protests

Year of Action	Type of Appl.	Number of Protests	Ave. Processing Time	Target Processing Time [1]	Approved	Cond. Approved [3]	Denied [3]	W/D
1985	Branch	2	72 days	45 days	2			
1986	Charter [2]	6	287 days	120 days	4	2		
	Branch	2	94 days	45 days	2			
	Merger	3	76 days	45 days	1	2		
1987	Charter [2]	3	339 days	120 days	2		1	
	Branch	5	158 days	45 days	5			
	Merger	5	113 days	45 days	5			
1988	Charter [2]	3	718 days	120 days	1			2
	Branch	4	268 days	45 days	4			
	Merger	4	218 days	45 days	1	3		

Notes - Processing Times

1. Target processing time for district processing of an application under delegated authority. Applications with a substantive protest cannot be decided by the district under delegated authority, but must be decided in Washington by the Senior Deputy Comptroller for Corporate and Economic Programs. The target processing time for Washington processing of those cases is 45 days, which is in addition to the district target processing time.

2. The charter applications represent applications for District of Columbia charters protested by the D.C. Reinvestment Alliance. Delays in decisions were related primarily to significant legal issues associated with these charters.

Notes - Decisions

3. In addition, during 1987, the OCC conditionally approved 8 applications based on CRA considerations where the application was not protested.

   In addition, during 1988, the OCC conditionally approved 8 and denied 2 applications based on CRA considerations where the applications were not protested.

Decisions - All Corporate Applications Covered by CRA

Year	Number of Actions	Approved	Conditionally Approved	Denied	Withdrawn
1987	2,195	2,085	49	17	54
1988	2,483	2,321	69	19	74

Other CRA Issues

Statement of the Federal Financial Supervisory Agencies Regarding the Community Reinvestment Act

In March of this year the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Federal Home Loan Bank Board, and the Federal Reserve Board adopted this CRA Policy Statement to provide guidance to institutions and community groups, and to clarify a number of issues that have arisen in enforcing the CRA.

For instance, institutions are presently required by regulation to prepare, annually update, and make available for public review a CRA Statement listing the loan products they are willing to offer. The new Policy Statement encourages each institution to significantly expand its CRA Statement to more accurately reflect the institution's overall approach to CRA, describing strategies for marketing and advertising, credit needs assessment and new product development, including past accomplishments and future plans. The size, resources and location of an institution will influence the degree of detail and the scope included in the expanded CRA Statement.

One of the main purposes of the revised Policy Statement is to shift the emphasis away from the corporate application process to build stronger and more ongoing mechanisms for outreach and service by institutions to their communities. We believe that the expanded CRA Statement is a better vehicle for doing that by focusing the attention of an institution's management, and of the public at large, on the institution's record on a continuing basis, and on any areas needing improvement.

In the revised Policy Statement we have encouraged community organizations to take advantage of the expanded CRA Statements as a starting point for discussion, bringing their concerns to the attention of an institution's management and to the appropriate supervisory agency as they arise, rather than in the adversarial atmosphere of a protest at the time of a corporate application.

Disclosure of CRA Ratings and Related Examination Comments

In light of these enhancements to the CRA assessment process, and the need for communities to be informed of banks' efforts with respect to their lending activities, including those in low- and moderate-income areas, the OCC would not object to the public disclosure of a narrative summary of a bank's performance under CRA. This will serve to increase the public's awareness of how well a bank is performing. These summaries should not be the same as the examination report comments, however. They would not include information of a confidential nature that is important for supervisory purposes, such as the financial condition of the institution, or any sensitive information about any of its employees, customers or members of the community.

Our objective is to inform the people of the community in a concise and forthright manner how well their local institutions are doing under the CRA. This will enhance the process initiated by the CRA Policy Statement by supporting ongoing and meaningful dialogue about CRA achievements and goals between the bank and its community.

Disclosure of CRA numeric ratings also has been proposed. As with safety and soundness ratings, CRA ratings historically have been held confidential by all the financial regulatory agencies. It is this agency's belief that such release would not serve the objective of keeping members of a bank's community informed of the bank's CRA performance. CRA ratings (like the other summary rating systems used by the banking agencies) serve an important, but limited, purpose for the supervisory agencies. In essence, the rating is the assignment of a quantitative value to the bank examiners' evaluation of a number of qualitative factors. It is an examiner's short-hand assessment of a bank's overall performance with respect to CRA and is only a general indicator of a bank's CRA performance.

In addition to the communication efforts encouraged in the CRA Policy Statement, the OCC issued Banking Circular 238, "Disclosure of CRA-related Corporate Application Decisions," on June 15, 1989. The circular revises procedures for disclosure of corporate application decisions where CRA performance was raised as a concern and provides easier access to the information for national banks and the public. The OCC will publish its decision letter when corporate applications from national banks have been conditionally approved or denied on grounds related to the CRA. The Office believes that publication of CRA-related decision letters will facilitate broader bank and public access to information on actions taken by the Office with respect to its statutory responsibilities. The decisions will also provide banks with additional guidance about how the Office uses assessments of bank CRA performance when deciding certain corporate applications.

Publication of CRA Examination Schedules

The Subcommittee has asked for our comments on the proposal to publish, in advance, the agency's CRA examination schedule. We assume that the purpose of this proposal is to provide greater opportunity for public input in the CRA examination process. We believe, however, that current procedures, including the use of a bank's public comment file, examiners interviews with community group members, and the use of expanded CRA Statements as encouraged by the new CRA Policy Statement, provide adequate opportunities for the public to communicate their concerns about bank CRA performance both to banks and their supervisory agencies. This process would not be enhanced, however, by the publication of the CRA examination schedule.

The scheduling of examinations is a very fluid process, subject to constant change and adjustment. When new issues or priorities arise, bank supervisors must have the flexibility to assign examiners to address them. Publication of an examination schedule would place the office in the untenable position of restricting this needed flexibility.

Summary and Conclusion

The OCC has developed a comprehensive program to encourage national banks to help meet the credit needs of their local communities. We believe that we have developed a program that strikes the right balance between the competing demands for our supervisory resources. We use on-site examination programs to make sure that national banks comply with the law. We train our examiners to assess national banks' compliance efforts and accomplishments. We consider the results of our assessments in evaluating corporate applications and are requiring national banks to strengthen their CRA performance. We maintain contacts with community and banking groups to help ensure that all parties understand the needs and resources of each other.

We believe that most national banks help meet the credit needs of their local communities in the ordinary course of doing business. The OCC has not found it necessary to deny many applications on CRA grounds. Denials are a last resort. They are used only when the far more effective tactic of conditional approval has little, if any chance, of improving bank performance.

The purpose of CRA is to encourage financial institutions to assess and help meet the credit needs of their communities, including the low- and moderate-income neighborhoods, by utilizing their own expertise and resources. The OCC believes that it has implemented appropriate systems for assessing the level of performance under the CRA; encouraged improvements to national banks' performance through examinations, education, outreach and communications activities; and enforced the spirit of the statute through the corporate application process.

A P P E N D I X 1

Other OCC Activities Related to the CRA

In addition to use of the examination and corporate application processes, the OCC, primarily through its Customer and Industry Affairs Division, also provides encouragement to banks through an ongoing program of educational and communications activities to help increase banking industry sensitivity to customer and community needs. These activities are designed to:

- Identify and assess key issues and concerns raised by bank customer groups and communicate these concerns to national banks through publications, banking issuances, advisories;
- Provide information to banks through conferences, roundtables and publications highlighting a variety of positive approaches and program models banks can and do use to help meet special credit needs in their communities and fulfill their CRA responsibilities; and
- Promote use of bank community development corporations and community development investments as one tool to help banks meet the community credit needs.

Outreach Activities

As part of the encouragement process, the OCC also coordinates activities to increase outreach with consumer and community groups, monitor CRA-related issues and offer feedback to the banking industry on issues and trends, including those related to the CRA. These activities help the OCC identify key issues concerning CRA enforcement and bank performance.

Formalized in 1984, OCC's outreach and monitoring program, through the Customer and Industry Affairs Division, includes: (1) regular contact with nationally-based bank customer groups (2) special meetings and briefings focused on key issues, (3) development of publications and other information to alert banks to issues and encourage their responsiveness, and (4) assistance to customer groups, banking organizations, government officials and other groups to develop their own programs focusing on bank participation in housing, community and economic development finance.

In addition, the OCC's six District Offices established outreach programs for contacting consumer and community groups, an bankers.

Major outreach activities have included:

- District Bank Customer Group Key Issues Meetings. In 1985, the OCC's Customer and Industry Affairs Division, in concert with District Offices, conducted Bank Customer Group Key Issues Meetings in each of the OCC's six Districts. The purpose of the meetings was to discuss a broad range of CRA, consumer, housing and small business issues and concerns and obtain customer group perspectives on bank and OCC performance. "Summary Reports" for each of those meetings were developed and provided to all national banks and selected customer groups in each respective District, and to key OCC policymakers and other federal regulatory agencies.

- National Bank Customer Groups Key Issues Meetings. Also, to obtain a broader, national perspective, the OCC arranged a "National Bank Customer Groups Key Issues Meeting" in April of 1986 which brought together the Comptroller, senior OCC management and representatives of nationally-based groups for a dialogue on banking issues affecting consumers, small businesses, community, civil rights, housing and state and local government organizations. A comprehensive summary of that meeting, which included a number of concerns national groups raised about CRA regulation and bank performance, along with OCC responses, was provided to all national banks, national customer groups, bank trade associations and other regulatory agencies. A similar meeting with nationally-based groups was held in November 1988.

- District Offices Community Outreach Program. In 1987 the OCC implemented a process under which District Offices conduct their own community outreach and contact programs to illicit customer group perspectives on bank performance under the CRA and other consumer compliance laws. Information collected through these outreach programs is utilized during the CRA examination process and in District Office communications with banks on compliance issues.

- Circulars and Advisories. Additional encouragement is provided to national banks through the issuance of special banking circulars and advisories. These alert banks to common issues and compliance concerns affecting national banks which the OCC has noted through examinations or its outreach and monitoring activities. CRA-related issuances have included:

  -- Banking Circular 189, "Branch Closings and Reductions in Service," which encouraged each national bank to develop and implement policies for branch closings to minimize adverse effects on the bank's community;

  -- Banking Circular 206, "Basic Banking Services," which encouraged national banks to provide basic banking services to their customers, including low- and moderate-income, young and retired persons who may be unable to pay regular charges for conventional banking accounts.

- Participation in Banking and Customer Group CRA-related Conferences/Programs. The OCC also provides ongoing assistance to banking organizations, customer groups, and other interested parties, to help them develop and implement informational programs and publications related to bank CRA compliance responsibilities and bank participation in special community financing programs. Over the last few years, OCC's activities have included the following:

  -- Comptroller Robert L. Clarke, senior OCC management and other OCC staff, have spoken at a number of conferences and workshops sponsored by the ABA, IBAA and other banking organizations on bank compliance and CRA issues

  -- The Office provided assistance to the ABA in developing a Branch Closings Manual, which was designed to help banks make informed decisions when branch closings become necessary.

  -- Each year, the Office assists the Securities and Exchange Commission to plan its annual small business Forum; in 1987, the SEC Forum focused on models and approaches used to provide equity and long-term financing for small businesses and included a number of bank-sponsored model programs.

  -- In November 1987, the Comptroller addressed a major conference sponsored by six national customer groups, "Community Rights and the Banking Industry", emphasizing the importance of the CRA and OCC's activities designed to encourage bank performance and accountability.

  -- Each year, the OCC assists many customer organizations to develop conferences and publications which feature sessions on bank CRA obligations and bank participation in community financing programs. Such assistance includes, provision of OCC speakers and informational materials, and advice on bank programs and speakers which could be featured. Among the organizations

assisted in 1987 and 1988 were the National Council for Urban Economic Development, the National League of Cities, the Southern Growth Policies Board, the Black Business Investment Board of Florida, the National Center for Policy Alternatives, National Peoples Action, ACORN, and the Consumer Federation of America.

OCC Conferences and Publications

In addition, the OCC sponsors a number of conferences and roundtables for bankers on CRA-related issues and community lending opportunities. One of the primary purposes of these meetings is to develop and provide information to national banks about the successful approaches banks have used in meeting community credit needs. In each case, a publication based on proceedings of the meeting is developed and provided by the OCC to national banks. Over the last few years these meetings and publications have included:

- Issues and Bank Initiatives in Low- and Moderate-Income Housing and Fair Lending. This major conference, held on June 15, 1989, brought together over 200 bankers, bank trade association and regulatory agency participants to discuss key issues banks face and model bank programs used to address low- and moderate-income housing credit needs. Comptroller Clarke was the keynote speaker. A publication based on the proceedings is now being developed and will be distributed to all national banks later this year.

- Community Development Finance: Tools and Techniques for National Banks. This publication, developed by OCC staff describes a variety of financing techniques and organizational models use by financial institutiwns to help meet important community credit needs in such areas as lower income housing, small and minority business development and neighborhood revitalization. The publication was sent to all national banks and OCC offices in March 1989. As of July 1, 1989, over 1,000 additional copies have been distributed in response to requests from banks and others.

- Bank Financing of Community Business Development. This roundtable, held in June 1988, addressed effective strategies for serving small businesses, particularly those owned and operated by minorities and women and those located in economically distressed areas. The roundtable brought together bankers and small business groups to discuss key financing issues faced by small businesses and strategies banks can use to address them. A publication

based on the roundtable proceedings was sent to all national banks.

- Opportunities and Issues for Banks in Affordable Housing, was a roundtable sponsored by the OCC In December 1986. The purposes of the Roundtable were to (1) heighten the awareness of bankers regarding opportunities for investment in affordable housing programs and (2) to highlight several effective financing programs offered by banks or through partnerships in which banks participate. The roundtable attracted more than 100 participants, the great majority of whom were bankers. Three panels addressed innovative approaches for bankers, public and other private sector leaders to work together to provide housing for low- and moderate-income people. A publication summarizing the proceedings was sent to about 2,000 national banks and almost 1,000 additional requests for the publication have been filled to date.

- The Changing Shape of Retail Banking: Responding to Customer Needs was a major national conference sponsored by the OCC in June 1985. Over 220 people attended including bankers, community, consumer and small business leaders and bank trade association representatives. The goal of the meeting was to help participants adapt to change and understand the evolving role of the bank customer. It was also meant to assist the OCC in understanding the concerns and needs of the industry and customer groups. A Conference publication was made available to customer group and banking organizations, and was sent to approximately 1,500 national banks.

- Small Business Lending and Private Secondary Markets. This roundtable, cosponsored with the National Federation of Independent Business (NFIB), in April 1984, highlighted innovative bank programs to make available long-term fixed-rate financing to smaller businesses. The purpose of the program was to educate bankers and leaders in the public and private sectors about opportunities and new approaches in small business finance and to encourage them to work together to implement creative long-term financing programs. It addressed new developments in the lending field with banks serving both as loan originators, and as sellers of loans to other investors with long-term investment horizons, such as pension funds. Approximately 50 leaders from the banking, small business and governmental sectors participated in the meeting. A publication based on the roundtable was produced by NFIB and was provided to 2,000 national banks.

OCC's Community Development Corporation Program for National Banks

Bank community development corporations and community development investments can be a useful tool in helping banks meet community credit needs. The Office of the Comptroller of the Currency administers and promotes the Community Development Corporation Program which allows national banks to make direct equity and other investments in community development corporations (CDCs), business ventures or community development projects serving predominantly civic, community or public purposes.

Through July 1, 1989, over 65 national bank CDCs and community development project investments have been approved by the OCC. Currently, there are 35 active CDC's and projects in which over 130 banks have made investments under the OCC's program. A number of CDCs have multiple bank investors.

National bank CDCs and community development investments have focused on low- and moderate-income housing development and rehabilitation, downtown and neighborhood commercial revitalization, industrial development and redevelopment, small and minority business assistance, neighborhood marketing, and training, technical assistance, research and planning for nonprofit development groups.

The OCC has initiated a number of activities designed to inform national banks about community development corporations and investments. Recent CDC activities by the OCC have included the following:

- Banking Circular 185. The Office issued Banking Circular 185 - "Community Development Corporations" in 1984. The Circular describes the OCC's policies, procedures and guidelines for national banks wishing to organize or invest in CDCs, or invest in community development projects.

- CDC Information Package. This package, entitled "Community Development Corporation Program for National Banks", was designed to provide national banks (and others) with important information on OCC's policies and procedures governing bank community development investments, and to encourage banks to consider such investments as part of their overall program to help meet community credit needs. The package included five separate pieces of information, each also used to help the OCC respond to specific requests

for information. These information pieces included:

-- CDC Brochure: "National Bank Community Development Corporations and Community Development Investments"

-- "Community Development Corporation Program Questions and Answers"

-- "National Bank Community Development Corporations: Directory"

-- National Bank Community Development Corporations: Background Information"

-- Banking Circular 185: Community Development Corporations.

Distributed initially in March 1987, the package has been used extensively by the OCC to respond to a growing number of bank requests for information about CDCs and community development investment options. In addition, upon request, the package, or individual pieces, were provided to customer groups, federal, state, and local government agencies, and a variety of bank and customer group trade associations for use at their conferences and other programs. To date, over 4,000 packages have been distributed to banks, customer groups and other interested parties.

- Financial Institutions' Community Development Corporations Forum, August 13, 1987 in Washington, D.C. To promote community development corporations, the OCC, together with the Board of Governors of the Federal Reserve System, convened this forum to provide information about bank CDCs and community development investments. The Forum was attended by over 200 individuals, including current Community Development Corporation (CDC) officials, bank and bank holding company representatives and others interested in establishing bank CDCs. The Forum included information on how to form a CDC and highlighted new and innovative housing and small business development approaches of current CDCs.

COMMUNITY REINVESTMENT ACT

TWELVE ASSESSMENT FACTORS	EXAMINATION PROCEDURES
1) Bank activities that ascertain the credit needs of its local community.	Obtain information from a review of bank records and interviews with bank staff. (Studies/customers/neighborhood groups/ local government)
2) The extent of the bank's marketing and special credit-related programs to make community members aware of credit services available.	Review bank's marketing program. (RE brokers/mtg counseling programs/ advertising/convenient hours/brochures)
3) The extent of participation by the bank's board of directors in formulating CRA policies and in the bank's CRA performance.	Review minutes of board of directors meetings and any other bank documentation available. (Bank staff awareness of CRA)
4) Any practices intended to discourage applications for credit listed in the bank's CRA statement.	Review other fair lending examination programs (ECOA and Fair Housing Act). (Bank staff awareness of CRA/prescreening)
5) The geographic distribution of the bank's credit extensions, credit applications and credit denials.	Initially rely on discussion with other examiners, review of examination reports and working papers of other programs. Review bank files and interview bank management. Additional reliance may be placed on preceding.
6) Evidence of discriminatory or other illegal credit practices.	Review prior reports of examination and other examination programs currently being performed.
7) The bank's record of opening and closing offices and providing services at offices.	Obtain information from the field or district office or from the bank's records. Review any public comments.

COMMUNITY REINVESTMENT ACT

(Continued)

TWELVE ASSESSMENT FACTORS	EXAMINATION PROCEDURES
8) Bank participation in local community development and redevelopment projects or programs.	Review written lending policy and procedure manuals. Interview lending officers. (HUD's community development block grant program/local neighborhood preservation efforts/CDCs/neighborhood housing services)
9) The bank's origination of residential mortgage loans, housing rehabilitation loans, home improvement loans, and small business or small farm loans within its community or the purchase of such loans originated within its community.	Review bank financial statements, HMDA disclosures, lending policy and procedure manuals. Interview bank staff.
10) Bank participation in governmentally insured, guaranteed, or subsidized loan programs for housing, small businesses or small farms.	Review bank financial statements, HMDA disclosures, lending policy and procedure manuals. Interview bank staff. (FHA/VA/ FmHA mortgage loans/SBA loans/FHA Title I home improvement loans)
11) The bank's ability to meet community credit needs based on its financial condition and size, and legal impediments, local economic conditions, and other factors.	Review examination workpapers and reports. Consider safety and soundness. (Small banks may lack resources)
12) Other factors that bear upon the extent to which a national bank is helping to meet the credit needs of its entire community.	Consider factors such as bank purchases of state and municipal bonds, secondary mortgage market securities or whether the bank's policies promote efforts to assist existing residents in neighborhoods undergoing reinvestment and change.

A P P E N D I X 3

UNIFORM INTERAGENCY CRA RATING SYSTEM

Composite Rating System

The performance categories are individually assigned a numeric rating. In Assigning the overall composite CRA rating, the performance categories will be evaluated according to how well the institution meets the following descriptive characteristics.

Rating (1)

The institutions in this group have a strong record of meeting community credit needs. Both the board of directors and management take an active part in the process and demonstrate an affirmative commitment to the community. Institutions receiving this rating normally rank high in all performance categories. Such institutions have a commendable record and need no further encouragement.

Rating (2)

Institutions in this group have a satisfactory record of helping to meet community credit needs. Institutions receiving this rating normally are ranked in the satisfactory levels of the performance categories. Such institutions may require some encouragement to help meet community credit needs.

Rating (3)

Institutions in this group have a less than satisfactory record of helping to meet community credit needs. The board of directors and management have not placed strong emphasis on the credit needs of the community. Institutions receiving this rating have mixed rankings surrounding the mid-range levels of the performance categories. Such institutions require encouragement to help meet community credit needs.

Rating (4)

Institutions in this group have an unsatisfactory record of helping to meet community credit needs. The board of directors and management give inadequate consideration to the credit needs of the community. Institutions receiving this rating generally rank below satisfactory in the majority of the performance categories. Such institutions require strong encouragement to help meet community credit needs.

Rating (5)

Institutions in this group have a substantially inadequate record of helping to meet community credit needs. The board of directors and management appear to give little consideration to the credit needs of the community. Institutions receiving this rating generally rank in the lowest levels of the performance categories. Such institutions require the strongest encouragement to help meet community credit needs.

PERFORMANCE CATEGORIES

I. Community Credit Needs and Marketing (Assessment Factors 1, 2, & 3)

Bank is evaluated on its activities in determining the credit needs of its community and marketing its services.

II. Types of Credit Offered and Extended (Assessment Factors 9 & 10)

Bank is evaluated on the types and amounts of credit extended and the degree to which those extensions are helping to meet the community's needs.

III. Geographic Distribution (Assessment Factors 4, 5 & 7)

The geographic distribution of the bank's loans and any practices meant to discourage applications are considered, as well as the impact of the opening or closing of any offices and the services offered at those facilities.

IV. Discrimination or Other Illegal Credit Practices (Assessment Factor 6)

The bank's compliance with anti-discrimination and other credit laws are evaluated. This rating must be the same as the overall compliance rating.

V. Community Development (Assessment Factors 8, 11 & 12)

The bank is evaluated for its participation in community development and/or factors relating to meeting local credit needs.

Senator DIXON. Thank you, Mr. McDowell.
Ms. Smith.

STATEMENT OF JANICE M. SMITH, DIRECTOR OF OFFICE OF CONSUMER AFFAIRS, FEDERAL DEPOSIT INSURANCE CORPORATION, WASHINGTON, DC

Ms. SMITH. Mr. Chairman, I am pleased to offer the views of the Federal Deposit Insurance Corporation on various matters related to the Community Reinvestment Act. The FDIC has worked hard since enactment of the CRA in 1977 to enforce the act and to encourage financial institutions to help meet the credit needs of their local communities, including low and moderate income neighborhoods.

The FDIC performs its role primarily through effective supervision and regulation of insured State chartered nonmember bank. We administer a compliance program by which about 9,000 FDIC-supervised banks are regularly examined, evaluated, and rated for compliance with the CRA and other consumer protection laws.

The FDIC has been increasing the number of compliance examinations conducted over the past few years. We completed over 1,200 compliance examinations in 1986, more than 2,200 in 1987, and nearly 3,100 in 1988. We estimate the number for 1989 will be about the same as in 1988.

The FDIC expects to continue to improve on this record as we hire and train more examiners to meet our increasing responsibilities.

The FDIC has approximately 2,000 field examiners, most of whom have received formal and on-the-job CRA training. We have at least one consumer affairs/civil rights review examiner in each of our eight regional offices. These examiners coordinate the FDIC's compliance efforts and are directly involved in examiner training. They also provide liaison for consumer and community groups and assistance to banks in assessing issues of community interest.

The FDIC's Division of Bank Supervision has further strengthened its compliance examination and enforcement efforts by designating a consumer compliance coordinator for each of its 94 field offices. These are commissioned examiners with compliance expertise who are responsible for overseeing the compliance examination and enforcement program in their respective field offices. They handle or coordinate the more complex compliance assignments and help train other examiners.

COMPLIANCE EXAMINATION DETAILS

Compliance examination details are also required of all commissioned and assistant examiners as part of their career progression. FDIC examiners evaluate the compliance with the CRA on the basis of a bank's attempt to ascertain determination to help meet and performance in helping to meet community credit needs in the context of the bank's resources and local circumstances.

The FDIC follows CRA examination procedures which were developed on an interagency basis. Particular attention is focused on the various assessment factors prescribed by regulation.

The FDIC rates banks in accordance with a uniform interagency CRA assessment rating system. About 98 percent of all FDIC-supervised banks examined for CRA compliance have been assigned satisfactory ratings.

It should be emphasized that the CRA rating reflects an assessment of a bank's performance record over time. Examiners discuss their findings regarding a bank's CRA performance with bank management and encourage them to make improvements where deficiencies or problems are noted.

Progressively more stringent administrative action is taken until compliance is achieved. Our overall experience has been that once a problem is brought to a bank's attention corrective measures are implemented in a timely manner.

FDIC policy provides that examiners should make outside contacts during regular compliance examinations when necessary to assess the bank's performance in meeting CRA goals. Community groups and other interested parties are also encouraged to contact the FDIC and banks on an ongoing basis concerning CRA and other consumer issues.

The public may call or write the FDIC's Office of Consumer Affairs or regional offices with complaints and inquiries.

During 1988, we received approximately 39,400 telephone calls for information and assistance, of which only about 300 involved community reinvestment matters. In 1988, nearly 3,600 written complaints and inquiries were received, only 20 of which involved CRA-related issues.

Our regulations require the maintenance of a public file of comments on a bank's CRA performance. This file is reviewed by examiners during the course of a CRA examination.

Community groups and other interested parties may learn about CRA covered applications filed with the FDIC through notices published in local newspapers for the convenience of the banking public. Interested parties may also learn about such applications for specific geographic areas by placing their names on regional office mailing lists for weekly notification.

Comments received concerning CRA-related issues are considered during the specified time periods. An extension of comment periods may be granted for good cause.

As part of the application process, community groups and other interested parties can request a public hearing or an informal proceeding. A decision on whether to hold a public hearing is based on how much new information is likely to be gained.

The FDIC has been successful in conducting informal proceedings with banks and community groups. Generally, major differences between the parties have been resolved without materially delaying the application process.

MONITORING AND ENFORCING

Monitoring and enforcing bank compliance with the CRA mandate is a critical component in the FDIC's evaluation of bank applications for deposit facilities. In making decisions on such applications, the FDIC gives due consideration to the bank's CRA performance record in all cases, not just when a protest has been filed.

The FDIC has received 19 CRA-related application protests since 1984. During the past 5 years, no applications have been denied based on CRA factors, one has been conditionally approved, 14 have been approved without conditions, and two were withdrawn.

The FDIC is aware of the importance of the CRA in encouraging banks to more comprehensively meet the credit needs of their entire communities. Effective enforcement by the FDIC is both essential and beneficial. It should be recognized, however, that implementation of the CRA must be accomplished in a manner that assures the safety and soundness of the financial institutions.

Thank you, Mr. Chairman, for giving the FDIC an opportunity to express our views on these issues. We would be pleased to respond to any questions.

[The complete prepared statement of Janice M. Smith follows:]

TESTIMONY OF

Janice M. Smith
Director
Office of Consumer Affairs

FEDERAL DEPOSIT INSURANCE CORPORATION
WASHINGTON, D.C.

ON

THE COMMUNITY REINVESTMENT ACT

BEFORE THE

SUBCOMMITTEE ON CONSUMER AND REGULATORY AFFAIRS
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE

2:00 p.m.
July 31, 1989
Dirksen Senate Office Building

FDIC
SUMMARY OF TESTIMONY
ON
THE COMMUNITY REINVESTMENT ACT
July 31, 1989

The FDIC regularly examines about 9,000 State-chartered nonmember banks for compliance with applicable consumer protection laws, including the CRA. Our goal is to examine banks rated 1, 2 or 3 for compliance at least every 24 months and 4 and 5 rated banks at least every 12 months, with visitations conducted as necessary. We conducted 1,228 compliance examinations in 1986, 2,242 in 1987, and 3,066 in 1988.

Compliance examinations are conducted by examiners who have received both formal and on-the-job training. Each of our eight Regional Offices have staff dedicated to the consumer compliance area. A Consumer Compliance Coordinator has been assigned to each of our 94 field offices and compliance details are required of all commissioned and assistant examiners.

The FDIC evaluates banks on a case by case basis using CRA examination procedures which were developed on an interagency basis. These procedures include assessment factors which are outlined in Part 345 of the FDIC's Rules and Regulations.

The FDIC rates banks in accordance with the Uniform Interagency CRA Assessment Rating System. About 98% of all FDIC-supervised banks examined for CRA compliance have been assigned satisfactory or better ratings. It should be emphasized that a CRA rating is an assessment of a bank's performance record over time. While individual instances of noncompliance are taken into account, a rating reflects a more comprehensive view of a bank's performance.

The FDIC uses examination ratings to summarize a bank's performance. It is a subjective judgment used for supervisory purposes. The FDIC does provide its ratings and the open section of examination reports to institutions under its supervision. For banks filing CRA-covered applications with the FDIC, a summary assessment of CRA performance is prepared and included in a public file at the applicant bank and appropriate FDIC Regional Office.

The FDIC may take various actions if noncompliance with the CRA is established, including: unsatisfactory ratings, memoranda of understanding, application denials, and ultimately a cease and desist order. Progressively more stringent administrative action is taken until compliance is achieved.

FDIC policy provides that examiners should make outside contacts during regular compliance examinations when necessary to assess a bank's performance in meeting community credit needs under the CRA. Community groups and other interested parties are also encouraged to contact the FDIC and banks on an ongoing basis concerning CRA and other consumer issues.

The FDIC publishes notices of applications in local newspapers. Each Regional Office also maintains mailing lists for weekly notification of applications filed. Comments received concerning CRA-related issues are considered during specified time periods. Extensions of comment periods may be granted for good cause.

Good afternoon, Mr. Chairman and members of the Subcommittee. I am pleased to offer the views of the Federal Deposit Insurance Corporation on various matters related to the Community Reinvestment Act "CRA".

Introduction

The FDIC has worked hard since enactment of the CRA in 1977 to enforce the Act's mandate. The objective is to encourage financial institutions to help meet local community credit needs, including those of low and moderate income neighborhood residents, consistent with the institutions' safe and sound operation. The FDIC performs its role primarily through effective supervision and regulation of insured state chartered, non-member banks. We administer a compliance program by which FDIC-supervised banks are regularly examined, evaluated and rated for compliance with the CRA and other consumer protection laws and regulations.

Today's testimony focuses on areas of particular interest to the Committee as outlined in the Chairman's letter dated July 6, 1989. These areas are discussed in the order of the questions presented in the letter.

1. Examination for Compliance with CRA

The FDIC administers a comprehensive consumer compliance examination program. FDIC-supervised institutions, numbering about 9,000, are regularly examined, evaluated and rated on their compliance with all pertinent consumer protection laws. The FDIC completed 1,228 compliance examinations in 1986, 2,242 in 1987 and 3,066 in 1988. We estimate the total number of compliance examinations for 1989 will be at about the same level as 1988. Banks are examined more frequently if they are rated less than satisfactory in CRA or overall compliance performance under the FDIC's examination policy. The goal is to examine banks rated 4 and 5 for compliance at least every 12 months, and banks rated 1, 2, or 3 at least every 24 months, with visitations conducted as necessary.

The trend in number of FDIC compliance examinations over the past three years is upward, even though the FDIC has had to devote significant resources to safety and soundness banking problems and, beginning in February 1989, to its interim supervisory role under President Bush's savings-and-loan rescue plan. In the future, we anticipate further progress in our compliance examination program.

In the CRA examination process, examiners evaluate banks on a case-by-case basis taking into account their size, expertise and location. Community credit needs often differ based on the characteristics of each local community. The FDIC uses CRA examination procedures (Attachment 1) which were developed on an interagency basis. These procedures include the assessment factors outlined in Part 345 of the Corporation's regulations. The assessment factors include but are not limited to: activities conducted by the bank to ascertain the credit needs of its communities and the bank's marketing of its services; the types of loans made; the impact of the opening or closing of any offices and the services offered at these facilities; the bank's compliance with anti-discrimination and other credit laws; and the bank's participation in community development in order to meet local credit needs.

The FDIC also considers complaints and inquiries in evaluating banks. During 1988, the FDIC's Office of Consumer Affairs and Regional Offices reported approximately 39,400 telephone calls for information and assistance, only 331 of which involved community reinvestment matters. Of 3,600 written complaints and inquiries only 20 involved CRA-related issues.

We do not believe public notice of CRA examinations would be practical. Public comments may not be received by the examiner prior to completion of the examination and at times examinations have to be rescheduled. Interested parties are encouraged to submit comments on an ongoing basis and not only when an examination takes place. Publication of CRA examination dates could discourage interim comments.

CRA is functionally integrated with other FDIC fair lending examination procedures. These include the Fair Housing Act (FHA), Home Mortgage Disclosure Act (HMDA), and the Equal Credit Opportunity Act (ECOA).

The use of HMDA data by FDIC examiners is important to help determine the possible existence of CRA and fair housing compliance problems. The HMDA Statement is generally considered a reliable indicator of the number and dollar amount of mortgage loans extended in a bank's lending area.

At times, a bank's HMDA Statement may reveal a disproportionately low number of loans in low or moderate income areas relative to other areas in the community. If this is found, examiners investigate further into the reasons for such patterns. Although a HMDA statement alone may not be sufficient to support violations of the CRA or other fair lending laws, a disproportionate lending pattern could serve as a basis for a less than satisfactory CRA rating.

The following list highlights some of the items which are used to evaluate CRA and fair lending compliance:

- The bank's public comment file
- Consumer complaints concerning the bank
- CRA Statements
- Actual CRA-related efforts undertaken by the bank
- The bank's loan, investment, and procedural manuals
- The community delineation and any supporting documents
- Previous compliance and safety and soundness examination reports
- Records regarding efforts to communicate with members of the bank's lending community, especially low and moderate income residents
- Fair housing monitoring information and log-sheets
- Aggregate and individual bank HMDA data
- Records of any special efforts to help meet the deposit service needs of low and moderate income residents, such as the offering of "lifeline accounts"
- All records of the bank's advertising efforts and content
- Adverse action notices (denials, terminations, or withdrawals), with special emphasis on protected groups and residents of low and moderate income neighborhoods

Examiners also evaluate efforts undertaken by banks to address the recommendations contained in the revised Statement of the Federal Financial Supervisory Agencies Regarding CRA, adopted by the FDIC in March of this year.

The credit needs of the community which a bank serves are determined in a variety of ways. HMDA data are used to ascertain the number and dollar amounts, and location of home loans made, which serve as a performance indicator. Market analyses undertaken by the bank are reviewed and local plans for communities and neighborhoods are also used when available. Credit needs may be determined by communicating with special interest and public service

organizations (both public and private), particularly those who work with low and moderate income neighborhoods. The extent of the bank's efforts to communicate with members of its community regarding the credit services it provides is also reviewed as is the involvement by the bank with real estate brokers, business opportunities brokers, and others who service low and moderate income neighborhoods.

Actual hours spent on CRA examinations may relate more to the type of bank (e.g., commercial vs. savings bank, wholesale vs. retail) than to asset size. For special CRA examinations which are conducted in response to a bank application or a protest, the number of hours expended may be higher than average. The following Table shows the average number of hours spent per examination on CRA compliance matters:

Average Hours Expended Per Examination on CRA
from 1985 through 1988 by Asset Size of Bank

Average Hours Per Exam	$0-50 million	$50-100 million	$100-500 million	Over $500
1985	4 1/2	6	10 1/2	24 1/2
1986	5	6 1/2	8	29
1987	5	5 1/2	8	16 1/2
1988	5	6 1/2	9	22

2. The FDIC's Examination Force

There is a total of 1,956 FDIC field examiners (as of 5/31/89), most of whom have received CRA training. The FDIC has at least one Consumer Affairs and Civil Rights (CA/CR) Review Examiner in each of its eight regional offices. These examiners coordinate the FDIC's compliance efforts and are directly involved in examiner training. They also provide liaison with consumer and community groups and assistance to banks in assessing issues of community interest.

The FDIC's Division of Bank Supervision is further strengthening compliance examination and enforcement efforts. A Consumer Compliance Coordinator has been selected for each of our 94 field offices. These are commissioned examiners with compliance expertise. Some of the duties of the Coordinator are to:

- Conduct, or assist in, compliance examinations and visitations; and meet with bank boards of directors in problem or unusual situations;
- Review, as necessary, certain compliance examination reports (e.g. compliance problems or unusual situations) prior to submission to the Regional Office;
- Oversee and coordinate responses to consumer complaints and inquiries;
- Conduct supplementary compliance training for examiners and serve as an instructor for Regional Office and the Division's Training Center compliance training programs;

22-155 O - 90 - 4

- Serve on Regional Office details and other assignments pertaining to the consumer compliance area.

To become commissioned, FDIC examiners must have passed a rigorous evaluation in the areas of safety and soundness and compliance generally after 3-6 years of on the job experience. Assistant examiners may, at times, be assigned to perform less complex compliance tasks primarily involving banks rated 1 and 2. FDIC policy is to assign its most experienced examiners and those who have specialized in the field of compliance examination to examine 3, 4, and 5 rated banks and to handle complex compliance matters. On-site CRA complaint and protest investigations are also assigned to these examiners.

The FDIC's CRA examination and investigation staff training is provided primarily in four ways. First, the FDIC's Division of Bank Supervision Training Center administers the Corporation's Consumer Protection School (CPS). Most CPS attendees are examiners with a minimum of two years bank supervision experience.

The following table provides data related to the CPS:

Year	Total Number of Sessions	Length of Each Session	Total # of FDIC Students	Hours of Fair Lending Training Per Session: CRA	FHA	ECOA	HMDA
1989	*8	5	---	--	--	--	--
1988	6	5	117	2	3	5	1
1987	4	5 Days	62	2	2	3	1
1986	3	8 Days	39	3.5	2	5	2

* Sessions scheduled for year.

Second, a two-hour overview of consumer protection and civil rights laws is included in the advanced training school for assistant examiners.

Third, the Office of Consumer Affairs also annually conducts a 2-3 day compliance seminar for Regional CA/CR Review Examiners and their assistants and/or field examiners. These Review Examiners also provide compliance training for their respective regional examination staffs. In addition, an advanced one week training program is being developed with approximately two days allocated to the CRA and related laws. The first session is scheduled for late 1989 and should be attended by 40-50 of our 94 regional field office Consumer Compliance Coordinators. These Coordinators will then provide training to regional examiners.

Fourth, in addition to formal training, regular compliance and CRA training is conducted on-site by senior field examiners. Our Regional Office staff keeps these examiners updated on all pertinent information relating to the scope of work assigned to them, including CRA-related information.

3. Assignment and Use of CRA Ratings

The FDIC rates banks in accordance with the Uniform Interagency CRA Assessment Rating System (Attachment 2). The ratings range from 1 to 5, with one being the best.

The aggregate CRA ratings assigned for examinations conducted during each of the past five years are as follows:

Year:	CRA Ratings: 1	2	3	4 and 5
1984	252	1,549	31	8
1985	98	947	22	3
1986	115	1,086	19	1
1987	221	1,965	40	8
1988	307	2,683	58	12

Note: Excludes Special Purpose Banks and Trust Companies not engaged in lending.

Recent statistics indicate that about 98 percent of all FDIC-supervised banks examined for CRA compliance were assigned satisfactory ratings, i.e., a 1 or 2. It should be emphasized that a CRA rating is an assessment of a bank's performance record over time. While individual instances of technical noncompliance are taken into account, ratings reflect a more comprehensive view of a bank's performance.

CRA ratings are based on performance. FDIC examiners evaluate compliance with the CRA on the basis of each bank's (1) attempt to ascertain, (2) determination to help meet, and (3) performance in helping to meet community credit needs in the context of an individual bank's resources and local circumstances. Examiners discuss their findings regarding the bank's CRA performance with bank management. Examiners also provide appropriate CRA-related information and technical assistance at that time, thereby helping banks to understand the purposes of the CRA and the FDIC's enforcement role. Overall, we believe our CRA enforcement efforts have been effective. This view is based on the large number of banks which are assigned a satisfactory or higher CRA rating, (i.e., a 1 or 2), the low number of CRA consumer complaints and protests we have received, and the few comments found in public files of FDIC-supervised banks relating to their CRA statement or CRA performance.

Banks find that noncompliance can lay the groundwork for CRA protests and complaints against them resulting in costly processing delays and possible denials of applications. Our overall experience, with few exceptions, has been that once a problem is brought to a bank's attention timely steps are taken to correct the deficiencies.

4. Citizen and Community Participation

FDIC policy provides that examiners should make the following outside contacts during regular compliance examinations when necessary to assess the bank's performance in meeting community credit needs under the CRA:

- Any person or organization that has, in a CRA comment to the public file, specifically requested to speak to an examiner;

- Any person or organization that has raised a substantial issue in a CRA comment letter which requires further explanation and/or verification -- such persons or organizations should be contacted even where they have not made a specific request for a meeting; and

- A representative sample of persons or organizations with whom the lender has said it communicated -- this form of outside contact would normally be made only in circumstances where there is a need to independently verify the lender's performance in ascertaining local credit needs.

Examiners are advised to make whatever other outside contacts are likely to provide valuable information concerning either the credit needs of the bank's community, its efforts to ascertain those needs and make known its credit services, or its efforts to meet those needs. Among the persons or organizations to be contacted, for example, might be local government community development officials who would normally be expected to have useful information concerning the types of development or redevelopment programs available in a community and the extent of the bank's participation.

The public may call the FDIC's Office of Consumer Affairs or Regional Offices during normal business hours, or write, with a complaint or inquiry. The Office of Consumer Affairs has a toll free number which, along with the agency's address, is well-publicized nationally in newspapers and public interest organization newsletters. In addition, FDIC's outreach efforts include representation at conferences or seminars sponsored by community and industry groups, where the attendees are encouraged to write and/or call whenever there is a perceived problem. During 1988, the FDIC's Office of Consumer Affairs and our Regional Offices reported approximately 39,400 telephone calls for information and assistance. Of this number, only 331 calls involved community reinvestment matters. In 1988, OCA and the Regional Offices processed nearly 3,600 written complaints and inquiries, only twenty of which involved CRA-related issues. The latter figure is consistent with prior years.

Community groups and other interested parties may learn about CRA covered applications filed with the FDIC through notices published in local newspapers for the convenience of the banking public. Interested parties may also learn about such applications for geographic area(s) of special interest by placing their names on Regional Office mailing lists for weekly notification.

The minimum processing time for relocation applications is 21 days, for mergers 30 days, and for all other applications, 15 days. The FDIC will delay processing if legitimate, substantive issues are raised which may have merit. Extensions of from 15 to 30 days may be granted in order to allow for submission of more detailed documentation or evidence.

The FDIC encourages interested parties to comment on applications within the time periods specified. This is important because timely comment allows the FDIC to carry out its responsibility to process applications within applicable time limits consistent with the public interest. Processing delays can be costly to banks and delay service to the community.

As part of the application process, community groups and other interested parties can request a public proceeding. The FDIC Regional Director decides whether to hold a public proceeding based on how much new information is likely to be gained from the process. Concurrence of the Washington Office is required if the Regional Director's decision is to deny a request for such a proceeding. Protests and complaints filed alleging CRA violations are not always concerned with CRA issues. Sometimes misunderstandings arise as to what is germane to the CRA and the FDIC's responsibilities in enforcing the CRA.

We have been successful in conducting informal proceedings with banks and community groups, and thereby have generally been able to resolve major differences between the parties without materially delaying the application process. Our goal, when presented with a CRA protest, is to encourage the parties to meet, discuss and satisfactorily resolve differences.

All CRA-related allegations are addressed in a formal statement accompanying the FDIC's order to approve or deny an application. These documents are available to the public for review. Where an application has been protested, the FDIC also sends a letter to the protestants explaining the action taken.

We believe that it is important to have regular dialogue with representatives from both community and consumer groups and the banking industry. Our outreach efforts include periodic meetings whereby community groups and consumer protection and civil rights organizations have an opportunity to meet with the Chairman and senior Corporation staff for an exchange of views on community reinvestment and other consumer and community-related issues. In addition, the FDIC conducts compliance seminars for bankers in various parts of the country, at which CRA concerns and other consumer-related laws and regulations are addressed.

5. Application Decisions

Monitoring and enforcing bank compliance with the CRA mandate is a critical component in the FDIC's evaluation of bank applications for deposit facilities. In making decisions on such applications, the FDIC gives due consideration to the bank's CRA performance record in all cases, not just when a protest has been filed. Action must be taken by the Director or Associate Director of the FDIC's Division of Bank Supervision where the requirements of CRA have yet to be favorably resolved (reflected by a 4 or 5 rating, or possibly a 3) or where a CRA protest has been filed. Applications may be submitted to the Board of Directors in these cases. The FDIC must resolve all statutory factors in determining whether or not the application will be approved.

Commitments for future action may be offered by the applicant as a means of assuring a stronger CRA record or resolving existing CRA issues. Such commitments are not viewed as part of the CRA record of performance of the bank, but may be given weight as an indicator of potential for improvement in the institution's performance. However, commitments made in the applications process cannot be used to overcome a seriously deficient record of CRA performance.

Where appropriate, the FDIC may require banks to take specific actions designed to improve CRA performance by granting conditional approval of an application. In such cases, approval granted by the FDIC generally becomes effective or final only after confirming that the bank has satisfied the appropriate conditions.

6. CRA Protests

The FDIC received no CRA-related application protests in 1984, two in 1985 (against two banks), two in 1986 (against two banks), nine in 1987 (against seven banks), five in 1988 (against five banks), and one (against one bank) thus far in 1989. During the past five years, no applications have been denied based on CRA factors, one has been conditionally approved, 14 have been approved without conditions, and two were withdrawn. In addition, we received six written complaints and inquiries in 1986, eight in 1987, twenty in 1988 and five so far in 1989. Investigations of each CRA complaint revealed no patterns or practices of discrimination. Also, FDIC examiners have found very few CRA comment letters in bank public files.

Since the Act's inception, the FDIC has denied three applications for deposit facilities due to CRA factors. The rate of application denials on CRA grounds, however, should not be given undue weight in assessing the FDIC's enforcement of the CRA. CRA-related problems often are corrected by banks at the request of the FDIC, prior to our action on an application. The incidence of such preapproval corrections has not been aggregated. Also, applications are sometimes withdrawn by applicants when it becomes clear that denial is likely.

The following table reflects actions on nonprotested CRA-covered applicatons for the years 1984 through the first half of 1989:

	1984	1985	1986	1987	1989	1st half 1989
Approved	1,580	1,402	1,515	1,750	1,801	839
Denied	21	12	8	10	4	1

The length of time it takes to process nonprotested applications ranges from an average of 30 days for branches and relocations to 111 days for deposit insurance. For protested applications, the average ranges from 40 days for relocations to 198 days for merger applications.

7. Supervisory Enforcement Actions

FDIC sanctions for noncompliance with the CRA include: unsatisfactory ratings, memoranda of understanding, application denials, and ultimately, a cease and desist order. Progressively more stringent administrative action is normally taken until compliance is achieved.

Examples of FDIC supervisory actions taken outside the application process against institutions not in compliance with the CRA are attached (Attachment 3). These include memoranda of understanding and a section 8(b) Cease and Desist Order.

Compliance with the terms of supervisory CRA-related enforcement actions and with commitments made in conjunction with a CRA covered application is enforced through visitations and through routine bank examinations by FDIC examiners. Whenever deficiencies are found in a bank's performance, they are pointed out and the bank is encouraged to promptly make appropriate corrections.

The FDIC does not enforce agreements made between the banks it supervises and groups or other interested parties. However, evidence presented that the agreement has been adhered to by the institution will be considered when assessing its record in meeting local credit needs.

8. Public Disclosure of CRA Ratings and Examination Reports

In regard to the public disclosure of CRA ratings and examination reports, we believe the release could:

- Deter open and frank discussions between a financial institution and its regulator;
- Have an adverse effect on institutions which have compliance problems but are trying to correct them; and
- Cause institutions to use the ratings and examination findings as an endorsement standard in advertising.

Community groups and other interested parties can monitor an institution's performance by obtaining the CRA statement, the HMDA data, interviewing consumers and meeting with bank personnel. In addition, summary CRA assessments are part of the public file for applications submitted to the FDIC and are provided to the public upon request.

The FDIC uses examination ratings to summarize a bank's performance. The ratings reflect a subjective judgment and are used for supervisory purposes only. The FDIC, FRB and the OCC do release aggregate CRA performance ratings to the public through the Federal Financial Institutions Examination Council (FFIEC). The FDIC also provides its ratings and the open section of examination reports to institutions under its supervision.

As an alternative to the public disclosure of CRA ratings and examination reports, we suggest that in addition to providing ratings and comments to institutions, the regulators also prepare a summary assessment without a rating, which the bank would be required to include in its public CRA file. The Regional Offices would also maintain these summary assessments which would be made available to the public upon request.

9. Notice of CRA Examinations

We do not believe public notice of CRA examinations would be practical. Even the most thorough CRA review usually takes only a few days. Publication near the date the examination commences may not allow for public comments to reach the examiner in a timely manner. Further, there are times when for very valid reasons, an examination must be rescheduled at the last minute. A notice requirement could cause confusion for the public and problems for regulators in these instances.

The regulatory agencies have complaint and CRA protest procedures in place which indicate where and to whom consumers may write to comment on an institution's CRA performance. Interested parties are encouraged to submit comments related to CRA to the regulatory agencies and financial institutions on an ongoing basis and not only when an examination is about to occur, which may be once every two years. Our regulations require the maintenance of a public file of comments on a bank's CRA performance, and this file is reviewed by examiners during the course of a CRA examination. A publication requirement could discourage interim comments, and thus be counter-productive.

Conclusion

The FDIC is aware of the importance of the CRA in encouraging banks to more comprehensively meet the credit needs of their communities and, in particular, the credit needs of low and moderate income neighborhoods. Effective enforcement by the FDIC is both essential and beneficial. It should be recognized, however, that implementation of the CRA must be accomplished in ways that assure the safety and soundness of financial institutions.

Thank you Mr. Chairman and members of the Subcommittee, for giving the FDIC an opportunity to express our views on these issues. We will be pleased to respond to any questions.

Attachments

COMMUNITY REINVESTMENT

INTRODUCTION

The Community Reinvestment Act (CRA) (12 U.S.C. 2901 et seq.) is intended to encourage banks to help meet the credit needs of their entire communities, including low- and moderate-income neighborhoods, while preserving the flexibility necessary to operate in a safe and sound manner.

Encouragement is to be provided by the Corporation which is required to:

- Use its examination authority to encourage a bank to help meet the credit needs of its entire community, consistent with the safe and sound operation of the bank;
- Assess, in connection with its examination, the bank's record of helping to meet the credit needs of its entire community; and
- Take that record into account in evaluating an application for deposit insurance, a branch or other deposit facility, office relocation or merger.

Proponents of the CRA were concerned, among other things, with situations in which local lenders reportedly exported local deposits to other areas despite sound local lending opportunities. Such disinvestment was considered a threat to community and neighborhood vitality. Lenders, therefore, are encouraged to give particular attention to local housing and development needs of urban and rural areas. Increased lender sensitivity to such needs would help preserve, rehabilitate and revitalize such areas. Moreover, even though credit for local housing and community development was emphasized, it was realized that other types of credit provide community facilities and services necessary for neighborhood vitality and, more generally, a healthy local community.

The CRA is not intended to inject hard and fast rules or ratios into the examination or application process. Rather, the law contemplates a judgmental evaluation of a lender's record in order to accommodate varying circumstances. Nor does the CRA require banks to make high risk loans that jeopardize their safety. Rebuilding and revitalizing communities are viewed as beneficial for both communities and banks.

PART 345 - COMMUNITY REINVESTMENT

The Corporation's implementing regulation (Part 345) requires the board of directors of each insured nonmember bank to adopt and, at least annually, review a CRA statement. The statement must include: (1) a delineation on a map of each local community served by the bank, (2) a list of the specific types of credit the bank is prepared to extend within each local community, and (3) a copy of the CRA notice. The regulation also encourages each bank to include in its statement a description of its efforts to ascertain and help meet community credit needs.

A bank must provide in each office a CRA notice, the exact wording of which is prescribed in the regulation. The public notice indicates that the CRA statement is available, that written comments on the statement and the bank's community lending performance may be submitted to the bank or the Corporation, that a file of such comments is publicly available, and that the public may request announcements of applications covered by the CRA from the Corporation. Each bank must keep a public file of CRA statements in effect and CRA-related public comments received during the past two years.

The CRA regulation sets forth a list of factors which the Corporation will consider in assessing each bank's record of helping to meet community credit needs, including those of low- and moderate-income neighborhoods. Banks are not required to adopt particular activities on the list since the regulation is designed to allow each bank considerable flexibility in determining how it can best help to meet the credit needs of its entire community in view of its particular skills and resources.

In essence, the regulation encourages banks to become aware of the full range of credit needs of their communities and to offer the types of credit and credit-related services that will help meet those needs. However, the regulation does not require banks to offer particular types or amounts of credit. The Corporation's assessment of a bank's CRA record will be taken into account by the Corporation in evaluating a variety of applications.

BACKGROUND FOR EXAMINATIONS

Judgmental Process

In conducting a CRA examination, the examiner is expected to adjust the CRA procedures on a case-by-case basis to accommodate banks that vary in size, expertise and locale. Community credit needs will often differ with the specific characteristics of each local community, and a bank should be evaluated on the basis of its attempts to ascertain, its determination to help meet, and its performance in helping to meet community credit needs in the context of its resources and local circumstances.

Balanced Viewpoint

The examiner should maintain a balanced perspective in conducting a CRA examination. The examiner cannot normally conclude on the basis of any one factor that a bank is or is not helping to meet the credit needs

of its local community or communities. Nor can the examiner adequately assess a bank's performance on the basis of any one source of information, data or opinion. For that reason, the examination procedures are designed to ensure that information from both the bank and the community is objectively reviewed and evaluated.

Bank's Input

The examination procedures give each bank the opportunity to demonstrate that it is having a beneficial influence on its local community or communities. Bankers that are helping to meet community credit needs are proud of that fact and will be of substantial assistance to the examiner in assessing the performance of their banks.

Examiner Encouragement

When appropriate, an examiner should encourage a bank to improve its CRA record by discussing with management various ways in which the bank may strengthen its performance. The examiner should not, however, insist on any specific action by the bank, such as the making of a certain type of loan, which would interfere with the bank's responsibility for establishing its own policies.

Examination Burden

The examiner must be careful to not unduly burden the bank since Congress did not intend to impose significant new reporting or recordkeeping requirements on banks. The examiner should normally request only required records and other existing information, but the scope of the review must always be sufficient for an adequate assessment.

Bank's Financial Condition and Size, Legal Impediments and Local Economic Conditions

A bank's ability to help meet community credit needs is influenced by its financial condition and size, as well as by any legal impediments and the local economic conditions under which it operates. An examiner must take these considerations into account in assessing the bank's performance and in providing encouragement.

Technical Compliance with the Regulation

The examiner will check for compliance with the specific requirements of the regulation. However, compliance with procedural requirements does not imply that the bank has been serving local credit needs. The converse is also true: noncompliance with a technical requirement does not necessarily mean that the bank is not helping to meet community credit needs.

The examiner must not lose sight of the intent of the statute in checking for technical compliance with the regulation. The entire examination is designed primarily to determine the extent to which the bank has helped and is helping to meet community credit needs.

Communication, Community Development and Low- and Moderate-Income Neighborhoods

In assessing the record, the examiner should bear in mind the special emphasis placed on effective communication and community development activities. With respect to communication, the premise is that community needs which can be met on a safe and sound basis are more likely to be met when the community is aware of the types of credit available and the lender is well informed about community credit needs. Hence, efforts to ascertain community credit needs and to publicize available credit services, including measures to identify the credit needs of, and to advertise in, low- and moderate-income neighborhoods, are encouraged. The examiner is authorized to conduct interviews with community members when such action would be appropriate in determining community awareness of the bank's credit services and local perception of credit needs.

The CRA also focuses on activities that foster development within the entire community, including low- and moderate-income neighborhoods. Consequently, housing-related extensions, participation in community development programs, and small business financing, including loans to small farms, are viewed favorably.

SELECTED FEATURES OF CRA EXAMINATIONS

The CRA Statement

A bank must prepare a separate CRA statement for each local community it serves, including a delineation of the relevant local community. It does not necessarily follow, however, that the statement prepared for each local community must contain a unique list of available credits. A bank serving several local communities may elect to prepare statements that contain lists of credits which are similar or identical for the local communities served. Since some credit needs are common to many local communities, such an approach would be consistent with the intent of CRA. There are other ways for a multi-community bank to satisfy this requirement. The examiner need not be especially concerned with the specific method employed by a multi-community bank so long as it makes a good faith effort to inform members of each local community about their community's boundaries and the types of credit extended there.

Reasonableness of Community Delineation

Each bank must delineate the local community or communities that it serves. For instance, a statewide

branching bank would serve a number of "local communities," the total of which would constitute its "entire community." Further, more than one office of a bank may serve the same local community. For example, a bank may have offices throughout a city and its suburbs and consider that entire metropolitan area to be the local community for those offices. Each community delineation must, of course, include the contiguous areas surrounding each office or group of offices.

Because many factors influence the size and shape of a bank's community, the regulation provides guidelines to assist each bank in defining its local community or communities.

The first guideline suggests the use of widely recognized existing boundaries such as those of MSAs or counties for delineating a bank's local community or communities. Such boundaries frequently constitute a reasonable approximation of a bank's local community.

In general, a local community based on existing boundaries should be no larger than an entire MSA or a county in a non-MSA area. If a bank has offices in more than one such area, it will have more than one local community. When a bank has an office near the boundary of an MSA or county, it should include those portions of adjacent counties that it serves. In rural areas, a local community may sometimes encompass more than one county but, generally, banks should not use states or regions of states to delineate local communities. A small bank that serves an area smaller than an MSA or county may define its community to be a part of the MSA or county. A bank may make adjustments in a community delineation in the case of areas divided by state borders, significant geographic barriers, or areas that are extremely large or of unusual configuration.

The second guideline proposes the use of effective lending territory, a concept more familiar to savings and loan associations than to commercial and mutual savings banks. The effective lending territory is that local area or areas around each office or group of offices where an institution makes a substantial portion of its loans and all other areas equally distant. If a bank employs its effective lending territory, it is encouraged to follow existing boundaries where practical.

One should not conclude from this guideline that each office necessarily serves a separate and distinct local community because each office typically has a different, though possibly partially overlapping, effective lending territory. If a bank is represented throughout a trade or market area, it may be more reasonable to use that area as its local community.

Finally, the regulation allows a bank to use any other reasonably delineated area. A bank is thus given substantial leeway in specifying its local community so long as the definition is reasonable; that is to say, the bank can provide a sensible rationale for the delineation and has not arbitrarily excluded any low- and moderate-income neighborhoods.

Low- and Moderate-Income Neighborhoods

In determining whether the community definition is reasonable, the examiner must be alert to situations where low- and moderate-income neighborhoods are gerrymandered out of a delineated area. Moreover, in assessing the record of a bank, the examiner should focus particular attention on its performance in low- and moderate-income neighborhoods within a local community.

Low- and moderate-income neighborhoods may be identified in most cases in a manner similar to the approach taken by HUD in administering the Community Development Block Grant Program. For this purpose, such neighborhoods are approximated by those census tracts in an MSA where median family income is less than 80 per cent of median family income for the entire MSA.

Unfortunately, these data are not available for non-MSA counties. Non-MSA areas, especially rural areas, present a particular problem in identifying low- and moderate-income neighborhoods. In those areas, the examiner may have to rely on personal knowledge of the area, physical inspection as necessary, discussion with bank personnel or a combination of these.

Small Business Lending

Small business loans represent one type of credit which the Corporation believes is directly related to the purposes of the CRA. In considering small business lending, the examiner should not be concerned with any hard and fast or precise definition of what constitutes a small business. Instead, the examiner should regard as small business lending any loans to local firms whose access to credit is limited to local sources because of their size.

EXAMINATION OBJECTIVES

1. To determine if the bank's policies address the intent of the CRA.
2. To encourage sensitivity and responsiveness to community credit needs.
3. To determine that the bank is complying with the requirements of the CRA regulation.
4. To determine the reasonableness of the bank's community delineation(s).
5. To assess the bank's record in helping to meet the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with a safe and sound operation.
6. To develop, organize and report information on the bank's record for use in the supervisory and application processes.

EXAMINATION PROCEDURES

Limited Review

1. Determine the method used by the bank to delineate its local community or communities and the reasonableness of each such delineation (345.3(a)) Note particularly any low- or moderate-income neighborhoods or areas that appear to have been arbitrarily excluded.

2. Assess the bank's record of performance in helping to meet the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with its safe and sound operation. The various assessment factors detailed in the regulation should all be considered to the extent applicable to the particular bank and the community or communities in which it operates. HMDA data should be used to ascertain the volume and location of housing loans. Particular attention should be paid to the relative volume of lending in low- and moderate income areas.

   In assessing the record, the examiner should review the Officer's Questionnaire, review and analyze the bank's public file and interview responsible personnel to determine efforts undertaken by the bank to ascertain and help meet community credit needs. To the extent necessary for an adequate assessment, the examiner is encouraged to interview community members to determine community awareness of the bank's credit services and local perception of credit needs as well as the bank's efforts to meet those needs.

3. Review each CRA statement in effect during the past two years to determine that all required items are included (345.4(b)) Note the specific types of credit the bank is prepared to extend within the local community and determine whether the types of credit in the CRA statement correspond with the types of credit actually being extended. Request an explanation of any difference.(345.4(b)(2))

4. Review minutes of directors' meetings to verify that all required CRA statements have been adopted, are reviewed at least annually and that the board has acted upon any interim changes and noted such actions in the minutes.(345.4(d))

5. Ascertain that the public file contains all signed comments received from the public that specifically relate to any CRA statement or to the bank's performance under the CRA as well as any responses made by the bank. The file should also contain all CRA statements in effect during the past two years.(345.5)

6. Ascertain that the bank's public notice contains the correct language and is properly posted (345.6)

7. Review with management the following:

   - The extent to which the bank is helping to meet the credit needs of its community;
   - Suggestions that might better enable the bank to help meet the credit needs of its community;
   - Deficiencies or exceptions in policies or practices; and
   - Procedural violations of the regulation.

Expanded Review

1. Ascertain from bank personnel what steps the bank has taken or plans to take which indicate whether it is helping to serve the credit needs of its local community or communities.

2. Obtain the following:

   - Minutes of the board of directors' meetings, particularly those dealing with the adoption, review and revision of all CRA statements.
   - The bank's files of public comments and recent CRA statements.
   - Comment letters received by the Corporation.
   - The bank's loan and investment policy and procedural manuals, along with other manuals relating to the CRA.

3. Review minutes of directors' meetings and verify that the board has:

   - Adopted a CRA statement for each delineated community.
   - Reviewed each statement at least annually.
   - Acted upon any material change in each statement at the first regular meeting of the board following the change.

4. Review and analyze the public files for:

   - Any signed, written comments received from the public during the past two years that specifically relate to any CRA statement or to the bank's performance in helping to meet the credit needs of its community or communities. Determine that the comments do not contain any material specifically prohibited by the regulation. However, the comments themselves should be considered.
   - Any responses to the commentors that the bank may have made.
   - All CRA statements in effect during the past two years.

   Note: Inherent in the process of reviewing public files is the option of contacting commentors and/or community members to the extent deemed necessary.

5. Review each CRA statement in effect during the past two years and:

   - Ascertain if the bank's delineation of its local community or communities is reasonable. Give special attention to the following:
     - Considerations used by the bank to define its community.
     - Community boundaries that are sharply asymmetrical, too narrowly drawn or so broad that the bank fails to focus on its local community.
     - Whether any low- and moderate-income neighborhoods have been arbitrarily excluded.
     - Public comments specifically relating to the reasonableness of the bank's delineation(s).
     - Any relevant information obtained from other examination programs that have been performed.

     If a question remains regarding the reasonableness of the community delineation, a review of community boundaries drawn by comparable local banks may provide useful information.
   - Review and analyze the specific types of credits within certain categories that the bank is prepared to extend within the local community. Determine if the types of credit in the CRA statement correspond to the types of credit actually being extended by the bank. Request an explanation of any differences. If feasible and appropriate, review the list of available credits prepared by comparable local banks.
   - Determine that a copy of the CRA public notice is included.
   - Analyze any of the following optional information that the bank may have included:
     - A description of how its efforts, including special credit-related programs, help to meet community credit needs.
     - A periodic report regarding its record of helping to meet community credit needs.
     - A description of its efforts to ascertain the credit needs of its community, including efforts to communicate with members of its community regarding credit services.
     - Any other material the bank may have included.

6. Analyze the bank's policies, procedures and operating practices to determine if the bank:

   - Provides the CRA public notice in a manner specified by the regulation. (A bank may reprint this notice as a poster or flyer to be placed in its lobby. The notice requirement may also be satisfied by making the CRA statement, which

includes the notice, available as a brochure in the lobby.)

- Makes all CRA statements available to the public as provided by the regulation.
- Makes the public comment files readily available for public inspection as provided in the regulation.

7. Review the bank's credit underwriting and appraisal criteria and the terms and conditions of loans to determine if they are being used for exclusionary purposes contrary to the objectives of the CRA.

8. Assessment Factors

- Activities conducted by the bank to ascertain the credit needs of its community, including the extent of the bank's efforts to communicate with members of its community regarding the credit services being provided by the bank.

  Ascertain from bank records and through interviews the extent to which the bank has communicated with members of its local community or otherwise has attempted to determine such needs. Pertinent factors may include:

  — Management review of written, signed comments received in response to the bank's CRA statement(s).

  — Studies conducted or reviewed by the bank concerning local credit needs.

  — The extent of the bank's efforts to communicate with members of its community regarding the credit services it is providing. Such members might include customers of the bank; educational organizations; merchants' associations; religious organizations; local government officials; block clubs; neighborhood organizations; coalitions of neighborhood organizations; local civil rights, consumer, minority, and non-English speaking groups; housing counseling service centers; community development corporations; nonprofit housing development corporations, and local development corporations.

  — The bank's communications with private organizations as may be identified by the Office of the Assistant Secretary for Neighborhoods, Voluntary Associations and Consumer Protection at HUD.

  — The bank's review of the local government's Community Development Plan and Housing Assistance Plan prepared in conjunction with HUD's Community Development Block Grant Program.

  — Economic forecasting, as developed or used by the bank.

- The extent of the bank's marketing and special credit-related programs to make members of the community aware of the credit services offered by the bank.

  Review the bank's marketing program and determine if it is adequately designed to encourage applications for loans in its community, particularly in low- and moderate-income neighborhoods. Pertinent factors may include:

  — Any working relationships the bank may have with real estate brokers or others who service low- and moderate-income neighborhoods.

  — Mortgage counseling programs and programs of management assistance for small or minority businesses.

  — Development and participation in mortgage review boards.

  — Credit and credit-related services in low- and moderate-income neighborhoods compared to such services in other neighborhoods served by the bank.

  — Use of bank representatives for seeking out potential housing-related and small business demand in low- and moderate-income neighborhoods.

  — Advertising the types of loans the bank is willing to make in media likely to reach low- and moderate-income individuals in the bank's local community or communities.

  — Availability of convenient hours in offices accessible to residents of low- and moderate-income neighborhoods.

  — Use of informational brochures and participation in other educational efforts.

- The extent of participation by the bank's board of directors in formulating the bank's policies and reviewing its performance with respect to the purpose of the CRA.

- Any practices intended to discourage applications for types of credit set forth in the bank's CRA statement(s).

  Review other fair lending examination programs, particularly as they pertain to interviewing and prescreening. Additionally, ascertain the following:

  — Whether administrative loan personnel and loan offices are aware of the CRA and the requirements of the implementing regulation.

  — Whether lending officers are aware of the bank's delineation of its local community or communities and its policies, if any, with respect to its commitment to help meet the credit needs of its entire community, including low- and moderate-income neighborhoods.

  — Whether loan officers are aware of the types of credit the bank offers to members of its local community or communities.

  — Whether public contact personnel are aware of the availability of the bank's CRA statement(s) and files of public comments.

  — Whether the bank is prepared to extend certain types of credit in some local communities or neighborhoods but not in others. An explanation of any difference should be requested.

  — The extent to which the bank is willing to make loans in its delineated local community or communities, utilizing information derived below. Special attention should be given to the specific reasons why loan applications have been denied, whether or not such denial has been on a prohibited basis.

  — Whether loan officers or other public contact personnel prescreen potential applicants from obtaining loans that the bank has stated it is willing to make, particularly applicants from low- and moderate-income neighborhoods.

- The geographic distribution of the bank's credit extensions, credit applications and credit denials.

  Determine whether there is any indication of a geographic distribution of credit extensions, applications for credit and credit denials which would signify failure to serve selected areas of local communities, particularly low- and moderate-income neighborhoods. Initial reliance may be placed on discussion with other examiners, review of reports of examination and work papers from other examination programs performed. For those banks located in MSAs, additional reliance may be placed on other fair lending examination programs for ascertaining the volume and location of housing-relating credits. For loans made outside MSAs, particularly with respect to banks that are not located in such areas, interview management and review internal files to determine the extent of housing-related lending in low- and moderate-income neighborhoods and the extent to which the bank has not extended such credit in these areas.

  Reliance may be placed upon geocoding of credit extensions, credit applications and credit denials. Where the bank is required to maintain logs of applications, the examiner should also review the logs to determine the geographic distribution of loans, applications and denials. In conjunction with other fair lending examination programs, it may be necessary to analyze further the geographic distribution of small business loans, including loans to small farms within the bank's local community.

- Evidence of prohibited discriminatory or other illegal credit practices.

  Review prior Compliance Reports and, in conjunction with other examination programs, determine the extent to which the bank is currently complying with the law.

- The bank's record of opening and closing offices and providing services at offices.

  Review the bank's record of and future plans for opening and closing branches and determine what factors management uses to determine which branches to close, which to leave open, and where to open new branches. The bank's approach can be determined through interviews with bank personnel knowledgeable about the bank's policy on opening and closing branches. Information can also be obtained through reviews of minutes of board of directors meetings, other bank records, Regional Office files, and interviews with representatives of public organizations with a particular focus on low- and moderate-income and minority neighborhoods. Also consider any information from interviews with community representatives about the attitudes of the community toward any actual or prospective branch closings.

  A review of the bank's branch record should include at a minimum the following items:

  — Any actions the bank has taken to minimize the impact of branch closings by trying to continue to offer services by alternate means, such as providing a way for customers to continue to obtain credit, installing ATMs or night deposit facilities, or by promoting continued productive use of the branch building.

  — Any attempts the bank has made to prevent closing any branches by adjusting hours, services, facilities, finding alternative sites

suitable to community residents, or the like in an attempt to make the branch viable.

— The bank's written plan for opening or closing its branches, if applicable. (Also review minutes of board of directors meetings for discussion of same.)

— The bank's system to account for expenses, income and profitability of branches and the application of this system to branch closings. (Also review minutes of board of directors meetings for discussion of same.)

— Any studies that may have been done to determine whether other financial institutions adequately serve neighborhoods where bank branches are or will be closed.

- The bank's participation, including investments, in local community development and redevelopment projects or programs.

  Review written lending policy and procedural manuals and interview lending officers to ascertain whether current programs include, or if the bank has considered involvement in, programs for satisfying potential credit needs such as the following:

  — HUD's Community Development Block Grant Program.

  — Local neighborhood preservation efforts.

  — Community Development Corporations.

  — Financing for Local Development Corporations.

  — Neighborhood Housing Services.

  — Investments in, or coordination with Minority Enterprise Small Business Investment Corporations (MESBICs), or Small Business Investment Corporations (SBICs) in providing loans to business for which equity or subordinated debt is provided by MESBIC or SBIC.

  — Purchase of securities of state and local housing agencies.

- The bank's origination of residential mortgage loans, housing rehabilitation loans, home improvement loans, and small business or small farm loans within its community, or the purchase of such loans originated in its community.

  Review the bank's financial statements, other appropriate records including HMDA statements, its written lending policy and procedural manuals, and interview lending personnel to ascertain whether the bank has originated or purchased such loans or has plans to do so.

- The bank's participation in governmentally insured, guaranteed, or subsidized loan program for housing, small business or small farms.

  This information may be obtained in ways similar to the ones in the assessment factor above. Examples of such government loan programs include:

  — FHA/VA/FmHA mortgage loans to members of its community or communities.

  — FHA Title I home improvement loans.

  — SBA loan guaranty programs.

  — Similar programs conducted by state or local agencies.

- The bank's ability to meet various community credit needs based on its financial condition and size, legal impediments, local economic conditions and other factors.

  The financial condition of the bank may be ascertained from discussion with other examiners or review of examination work papers and reports. Small banks may not have the specialized staff or financial resources needed to participate in some loan programs.

  Legal restrictions on permissible activities, interest rates, and branches may affect a bank's ability to help meet community credit needs. Adverse economic conditions caused by local or general economic difficulties may force a bank to temporarily curtail its lending activities.

  Other factors may affect a bank's ability to help meet community credit needs.

- Other factors that in the Corporation's judgment reasonably bear on the extent to which the bank is helping to meet the credit needs of its entire community.

  Pertinent factors may include:

  — Purchases of state and municipal bonds, secondary mortgage market securities, or such other activities when they further special purposes in the community, such as the construction or rehabilitation of low- and moderate-income housing or other neighborhood or community development, or are issued by municipalities or other local public financing units which do not have access to the capital markets.

  — Whether the bank's policies promote efforts to assist existing residents in neighborhoods undergoing a process of reinvestment and change.

  — Whether the bank offers "basic financial services" such as low cost transaction and savings accounts with low or no minimum balances, accounts for consumers who use a limited number of checks or drafts, and other accounts on which minimal charges are made for account maintenance. The marketing efforts for these types of accounts should also be evaluated.

  — Any other relevant factors.

In some instances, it may prove beneficial or necessary to the assessment process to contact persons or organizations outside the bank to help determine the bank's record of meeting community credit needs and to identify unmet credit needs. The following are examples of types of outside contacts the examiner should normally make:

- Any person or organization that has specifically requested to speak to an examiner on a CRA or fair housing lending matter;

- Any person or organization that has raised in a CRA comment letter a substantial issue which requires further explanation or verification;

- A sample of persons or organizations with whom the bank has said it communicated. (This form of contact, however, should usually be made only in circumstances where the examiner determines a need to independently verify the bank's efforts to ascertain local credit needs.)

- Where there are indications of prescreening on the basis of race or sex or other disparate treatment of minorities or women, any person or organization that is likely to receive complaints or other information concerning such treatment.

- Any other person or organization likely to provide valuable information concerning the credit needs of the bank's community, its efforts to ascertain those needs and make known its credit services, or its efforts to meet the credit needs of the community. Examples include local community development officials, real estate brokers, city and county officials, chambers of commerce, community action groups, local business persons and clergymen.

Initial contact may be made by telephone and suffice as adequate in some instances. An in-person interview should be conducted, however, whenever considerable information is likely to be provided, a number of people may be interviewed at the same location or relevant documentation may be made available for review. Outside contacts should be documented either in the workpapers or in the supervisory section of the Compliance Report, including the names and titles of the persons and/or organizations contacted and a brief summary of their comments regarding the bank's record of performance in the community.

9. Determine if the bank's record of performance demonstrates a recognition of its continuing and affirmative obligation to help meet the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with safe and sound operation.

10. Review the following with management:

    - The extent to which the bank is helping to meet the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with safe and sound operation.

    - Suggestions that might better enable the bank to help meet the credit needs of its entire community.

    - Procedural violations of the regulation.

    - Deficiencies or exceptions in policies or practices.

RATING SYSTEMS

CONSUMER COMPLIANCE RATING SYSTEM

The primary purpose of the rating system is to help identify those institutions whose compliance with consumer protection and civil rights statutes and regulations display weaknesses requiring special supervisory attention and which are cause for more than a normal degree of supervisory concern. To accomplish this objective, the rating system identifies an initial category of institutions that have compliance deficiencies that warrant more than normal supervisory concern. These institutions are not deemed to present a significant risk of financial or other harm to consumers but do require a higher than normal level of supervisory attention. Institutions in this category are generally rated composite "3". The rating system also identifies certain institutions whose weaknesses are so severe as to represent, in essence, a substantial or general disregard for the law. These institutions are, depending upon the nature and degree of their weaknesses, rated a composite "4" or "5".

In assigning the composite rating, all relevant factors must be evaluated and weighed. In general, these factors include the nature and extent of present compliance with consumer protection and civil rights statutes and regulations, the commitment of management to compliance and its ability and willingness to take the necessary steps to assure compliance, and the adequacy of operating systems, including internal procedures, controls, and audit activities designed to ensure compliance on a routine and consistent basis. The assignment of the composite compliance rating may incorporate other factors that impact significantly on the overall effectiveness of an institution's compliance efforts.The Corporation has devised a three dimensional rating scheme designed to assist examiners in arriving at a more meaningful analysis of the bank's compliance posture prior to assigning the composite consumer compliance rating. The specific dimensions comprising the Corporation's rating schemes are:

M - Management V - Violations and
P - Program or "MVP"

All ratings are assigned on a scale of 1 through 5 in ascending order of supervisory concern. Thus, "1" represents the highest rating and consequently the lowest level of supervisory concern; while "5" represents the lowest, most critically deficient level of performance, and therefore the highest degree of supervisory concern. Each bank is accorded a composite consumer compliance rating which reflects the overall performance of the bank on the basis of the three dimensions.

The MVP individual ratings are to be assigned on the basis of the following specific guidelines. These guidelines, however, do not preclude consideration of other factors which, in the judgment of the examiner, are deemed relevant to accurately portray the rating of the individual dimension.

Management

One
Management displays a positive attitude toward compliance and is capably administering an effective compliance program. Changes in consumer laws and regulations are promptly addressed in the bank's policies, and violations and deficiencies receive immediate corrective action.

Two
Management is adequately overseeing the bank's compliance program. Problem areas are few in number and easily corrected. Review of prior reports indicates a willingness to effect correction of violations. If required, reimbursements are made voluntarily.

Three
Management is not devoting sufficient time to the administration of the bank's compliance program and previously identified violations remain uncorrected. Although knowledgeable of the requirements of the various laws and regulations, increased efforts are required to effectuate compliance.

Four
Management has not exerted sufficient effort to ensure compliance with the various laws and regulations. There is a lack of interest or capability in administering a compliance program which has resulted in numerous repeat violations.

Five
Management has demonstrated an unwillingness or inability to operate within the scope of consumer laws and regulations. Serious problems remain uncorrected and management's attitude towards compliance is poor.

Violations

One
Violations, if any, are technical and easily corrected. There is no evidence of discriminatory acts or practices and there are no repeat violations.

Two
Any violations noted involve technical aspects of the law, or result from oversight or clerical error on the part of operating personnel. There is no evidence of discriminatory acts or practices and no reimbursable violations. Any repeat violations are few in number and technical in nature.

Three
Reimbursements, if present, involve several customers and are minimal in amount. There is no evidence of discrimination; however, violations may be numerous. Patterns of repeat violations may exist.

Four
Numerous violations are present and reimbursements, if any, affect a significant number of customers and are substantial in amount. Discriminatory acts or practices may be in evidence. Practices resulting in violations cited at previous examinations remain uncorrected.

Five
The bank is in substantial noncompliance with most consumer laws and regulations. Discrimination, numerous reimbursements and/or practices resulting in repeat violations are present.

Program

One
An effective compliance program, including a system of internal procedures and controls, has been established. Recordkeeping systems and employee training arrangements are good. Changes in laws and regulations are promptly reflected in the bank's compliance program and procedures for handling consumer complaints are in place.

Two
Although a system of internal controls and operating procedures has been established to ensure compliance, violations have nonetheless occurred. Modifications in the bank's compliance program and/or establishment of additional review/audit procedures may be warranted. Personnel appear knowledgeable of compliance matters and training is satisfactory.

Three
Operating controls and procedures have not proven effective and require strengthening. Training is inconsistent and knowledge of regulations is weak in some areas. Management is not sufficiently involved in the compliance program to effect favorable changes.

Four
The compliance program is not effective and internal procedures and controls are seriously deficient. Personnel lack knowledge in several critical areas and there is no formal training. Management is not actively involved in administering the very rudimentary compliance program in place.

Five
There is no compliance program, written or oral. Knowledge of the laws and regulations is extremely limited and problem areas remain uncorrected.

For convenient reference, a chart depicting the characteristics of each rating dimension is provided on the following page.

CONSUMER COMPLIANCE
RATING SYSTEM CHART

MANAGEMENT	ONE	TWO	THREE	FOUR	FIVE
	Policies strong - Operation - Controls - Compliance	Adequate over-sight - Minor deficiencies correction	Operation fair - Improvement necessary	Weaknesses - Policy/Control effort	Lacking - Inadequate - Poor results
VIOLATIONS					
Type/Volume	Technical/None	Technical - isolated or not numerous	Substantive - May be numerous	Substantive - Numerous	Substantive - Most regulations
Repeat	None	Few and technical	Once or more - patterns may exist	Existing exist	Patterns exist
Reimbursable	None	None	Several customers - several amounts	Significant number of customers - Substantial amounts	Numerous patterns - Substantial amounts
Apparent Discrimination	None	None	None	May be evident	Evident
PROGRAM	Effective	Some exceptions occur	Limited effectiveness	Seriously deficient	None

COMPOSITE RATING

Taking into consideration the MVP ratings, and other factors as warranted, a composite consumer compliance rating should be accorded. These ratings are defined and distinguished as follows:

One
An institution in this category is in a strong compliance position.
Management is capable of and staff is sufficient for effectuating compliance. An effective compliance program, including an efficient system of internal procedures and controls, has been established. Changes in consumer statutes and regulations are promptly reflected in the institution's procedures and compliance training. The institution possesses adequate training for its size and complexity, and personnel relate to relatively minor deficiencies as they arise. Violations that are cited are easily corrected. There is no evidence of discriminatory acts or practices, reimbursable violations, or practices resulting in repeat violations. Violations are promptly corrected by management. As a result, the institution gives no cause for supervisory concern.

Two
An institution in this category is in a generally strong compliance position.
Management is capable of administering an effective compliance program. Although a system of internal operating procedures and controls has been established to ensure compliance, violations have nonetheless occurred. These violations, however, involve technical aspects of the law or result from oversight on the part of operating personnel. Modifications in the bank's compliance program and/or the establishment of additional review/audit procedures may eliminate many of the violations. Compliance training is satisfactory. There is no evidence of discriminatory acts or practices, reimbursable violations, or practices resulting in well-defined patterns of repeat violations.

Three
Generally, an institution in this category is in a less than satisfactory compliance position.
Banks in this category are a cause for supervisory concern and require more than normal supervision to remedy deficiencies. Violations may be numerous. In addition, previously identified practices resulting in violations may remain uncorrected. Overcharges, if present, involve a few consumers and are minimal in amount. There is no evidence of discriminatory acts or practices. Although management may have the ability to effectuate compliance, increased efforts are necessary. The numerous violations discovered are an indication that management has not devoted sufficient time and attention to consumer compliance. Operating procedures and controls have not proven effective and require strengthening. This may be accomplished by, among other things, designating a compliance officer and developing and implementing a comprehensive and effective compliance program. By identifying an institution with marginal compliance early, additional supervisory measures may be employed to eliminate violations and prevent further deterioration in the institution's less than satisfactory compliance.

Four
An institution in this category requires close supervisory attention and monitoring to promptly correct the serious compliance problems disclosed.
Numerous violations are present. Overcharges, if any, affect a significant number of consumers and involve a substantial amount of money. Often practices resulting in violations and cited at previous examinations remain uncorrected. Discriminatory acts or practices may be in evidence. Clearly, management has not exerted sufficient efforts to ensure compliance. Its attitude may indicate a lack of interest in administering an effective compliance program which may have contributed to the seriousness of the institution's compliance problem. Internal procedures and controls have not proven effective and are seriously deficient. Prompt action on the part of the supervisory agency may enable the institution to correct its deficiencies and improve its compliance position.

Five
An institution in this category is in need of the strongest supervisory attention and monitoring.
It is substantially in noncompliance with the consumer statutes and regulations. Management has demonstrated its unwillingness or inability to operate within the scope of consumer statutes and regulations. Previous efforts on the part of the regulatory authority to obtain voluntary compliance have been unproductive. Discrimination, substantial overcharges, and/or practices resulting in serious repeat violations are present.

UNIFORM INTERAGENCY COMMUNITY REINVESTMENT ACT (CRA) ASSESSMENT RATING SYSTEM

Introduction

The purpose of the rating system is to provide a uniform means for regulatory agencies to identify quickly those institutions which require varying degrees of encouragement in helping to meet community credit needs. This provides a comprehensive and uniform system for evaluating the performance of federally regulated financial institutions examined under the various assessment factors of the Community Reinvestment Act and facilitates more uniform and objective CRA ratings.

The rating system ranks financial institutions on a scale from 1 through 5 with a "5" representing the lowest level of performance under the Act and, therefore, the highest degree of concern. Level "3" reflects performance which is less than satisfactory.

This system further employs five "performance categories" or components from which the overall composite CRA rating is derived. The performance categories represent a grouping of the various assessment factors contained in the implementing regulation for the Act. Each performance category is evaluated on a scale of 1 to 5 with a "5" representing the lowest level and therefore the worst performance. As explained later, each performance category includes a narrative description for each rating level.

Overview

Each financial institution is assigned a composite CRA rating that is based upon the institution's performance in meeting various community credit needs. An examiner begins to evaluate the institution's record in meeting community credit needs by first reviewing its financial condition and size, legal impediments, and local economic conditions, including the competitive environment in which it operates. The type of community in which the institution is located will also have a significant bearing on how the institution fulfills its obligations to the community. Community credit needs will often differ with the specific characteristics of each local community, resulting in a variety of ways an institution may meet those needs. To maintain a balanced perspective examiners must carefully consider information provided by both the institution and the community.

Composite Rating

The performance categories are individually assigned a numeric rating. In assigning the overall composite CRA rating, the performance categories will be weighed and evaluated according to how well the institution meets the descriptive characteristics listed below.

Rating (1) — The institutions in this group have a strong record of meeting community credit needs. Both the board of directors and management take an active part in the process and demonstrate an affirmative commitment to the community. Institutions receiving this rating normally rank high in all performance categories. Such institutions have a commendable record and need no further encouragement.

Rating (2) — Institutions in this group have a satisfactory record of helping to meet community credit needs. Institutions receiving this rating normally are ranked in the satisfactory levels of the performance categories. Institutions in this category may require some encouragement to help meet community credit needs.

Rating (3) — Institutions in this group have a less than satisfactory record of helping to meet community credit needs. The board of directors and management have not placed strong emphasis on the credit needs of the community. Institutions receiving this rating have mixed rankings surrounding the mid-range levels of the performance categories. Such institutions require encouragement to help meet community credit needs.

Rating (4) — Institutions in this group have an unsatisfactory record of helping to meet community credit needs. The board of directors and management give inadequate consideration to the credit needs of the institution's community. Institutions receiving this rating generally rank below satisfactory in the majority of the performance categories. Such institutions require strong encouragement to help meet community credit needs.

Rating (5) — Institutions in this group have a substantially inadequate record of helping to meet community credit needs. The board of directors and management appear to give little consideration to the credit needs of the institution's community. Institutions receiving this rating generally rank in the lowest levels of the performance categories. Such institutions require the strongest encouragement to be responsive to community credit needs.

Performance Categories

For purposes of evaluating an institution's CRA performance the various assessment factors and criteria are grouped into the following "performance categories":

I. Community Credit Needs and Marketing
The institution is evaluated in this category on its activities in determining the credit needs of its community and in marketing its services. Included in this category are assessment factors (a), (b) and (c) in addition to how well the institution delineated its community and other technical compliance regarding the posted notice and maintenance of public files.

II. Types of Credit Offered and Extended
The institution is evaluated in this category on the types and amounts of credit extended to the community and the degree to which those extensions are, in fact, helping to meet the community's needs. Included in this category are assessment factors (i) and (j) plus the institution's CRA statement.

III. Geographic Distribution
The geographic distribution of the institution's loans and any practices meant to discourage applications are considered in this category, as well as the impact of the opening or closing of any offices and the services offered at those facilities. Included in the category are assessment factors (d), (e) and (g).

IV. Discrimination or Other Illegal Credit Practices
The institution's compliance with anti-discrimination and of the credit laws is evaluated in this category. The category includes assessment factor (f). The rating to be assigned here corresponds to the institution's composite compliance rating.

V. Community Development and Other Factors
The institution is evaluated in this category on its participation in community development and/or other factors relating to meeting local credit needs. Included in this category are assessment factors (h), (k) and (l).

Each of the performance categories and the level of performance relating to each category are described in greater detail below.

Performance Category Ratings

I. Community Credit Needs and Marketing
(Assessment Factors (a), (b), (c) and Community Delineation)

Rating Level 1 — The institution has actively undertaken steps to determine community credit needs. These activities may include:

- Identifying the demographic makeup (racial/ethnic groups and low- and moderate-income areas) of its community and making meaningful contacts with a reasonably full range of organizations (civil, religious, neighborhood, minority, etc.) to assist in determining the credit needs of all segments of its community;
- Taking into consideration comments to the public file which describe existing unmet credit needs; and
- Contacting local government officials to identify any needs of private lender participation in existing or prospective community development or redevelopment programs. (In rural areas the local government body may be the county supervisor's office or other appropriate office.)

The institution has actively undertaken marketing and credit related programs appropriate to the size and capacity of the institution and the nature and location of the community. These programs should reach all segments of its community. Community segments should include low- and moderate-income residents, small businesses and, where applicable, owners of small farms. Management has also established working relationships with real estate brokers and others who serve low- and moderate-income areas and who may provide assistance for small or minority businesses. There is evidence that senior management is aware of community concerns and activities.

Rating Level 2 — The institution has undertaken activities to determine its community's credit needs. As a result of these activities, the institution is generally aware of the credit needs within its community, including low- and moderate-income areas. The institution has initiated a dialogue with community representatives such as local government, neighborhood, religious, and minority organizations, or small business and small farm organizations. The institution has undertaken marketing and credit related programs but the programs are not ongoing or comprehensive. Senior management demonstrates an awareness of community concerns and activities.

Rating Level 3 — The institution's activities to determine community credit needs are limited. The institution's employees may serve as volunteers on community organization boards and committees. However, the institution has not established a systematic method to determine how or if its employees' volunteerism assists the institution in meeting its CRA goals. The institution's advertising may be principally deposit oriented. In addition, the institution generally has made no efforts to market its services on an equal basis to all segments of its community. Marketing and credit related programs do not include a mechanism for reaching low- and moderate-income areas within the delineated community. The institution's marketing effort does not adequately focus on marketing the types of credit for which the institution has identified a need (or a need is otherwise apparent). There may also be some concern about the community delineation.

Rating Level 4 — The institution's efforts to determine community credit needs are very limited and fail to address major segments of its community. Management has not established a dialogue with organizations representative of the community, including any which represent low- and moderate-income or minority neighborhoods within the delineated community. The institution's marketing and credit related programs are limited or poorly conceived. There may also be some concern about the community delineation. Senior management is unaware of special needs of low- and moderate-income residents, small business and small farms.

Rating Level 5 — The institution has not undertaken any meaningful efforts to determine community

A
Appendix

credit needs. Management has limited knowledge regarding the community's demographic characteristics. The institution's marketing and credit related programs are either non-existent or have repeatedly excluded low- and moderate-income areas within the delineated community. There may also be some concern about the community delineation.

II. Types of Credit Offered and Extended (Assessment Factors (i), and (j) and CRA Statement)

Rating Level 1 — The institution has investigated the need for different types of credit within its community such as residential mortgage loans, housing rehabilitation and home improvement loan, and small business or farm loans, including the need for private, as well as, government-insured, guaranteed, or subsidized forms of such loans. It has then made an explicit effort to assure that its loan policies are responsive to the needs and has examined the extent to which it and other institutions within the community are meeting the need for such loans. The institution's CRA statement lists the types of loans found to be needed in the community. The involvement by the institution in the making of each type of loan listed in the statement demonstrates an affirmative effort to make such loans and to do its share in meeting existing needs, consistent with its resources and capabilities.

Rating Level 2 — The institution's CRA statement and loan portfolio indicate that it has investigated the need for residential mortgage loans, housing improvement/rehabilitation loans, small business and farm loans, and private, as well as government-insured, guaranteed, or subsidized forms of such loans within its community. It has made an explicit effort to assure that its loan policies are responsive to the needs found. The institution's performance in this category is distinguished from a 1-rated institution primarily in the extent to which it is marketing the availability of loans and/or in the degree to which the types and volume of loans being made match the community's most pressing credit needs.

Rating Level 3 — The institution may not be offering one or more types of credit listed in its CRA statement, despite a capacity to do so. The institution's loan portfolio and other sources, including peer analysis, may indicate that the institution's share of loans of a type or types identified as needed in the community, including any low- and moderate-income areas, is marginal or somewhat below average, particularly with respect to extensions for residential housing, small business or farm credit.

Rating Level 4 — The institution's record of offering and of making loans reveals that it is doing relatively little to help meet known or demonstrated credit needs for residential, small business or small farm credit, particularly for residents of low- and moderate-income areas. Its participation in private, as well as government insured, guaranteed or subsidy loan programs is either prefunctory or nonexistent, under circumstances where the need for such loans has been identified and the lender can articulate no objective supportable reason for its low level of participation.

Rating Level 5 — The institution is unwilling to adapt its credit offerings to serve demonstrated unmet credit needs in its community, particularly for housing, small business or small farm credit. This rating would be particularly appropriate where the lender's failure to meet these needs was cited in a previous examination.

III. Geographic Distribution (Assessment Factors (d), (e) and (g))

Rating Level 1 — The geographic distribution of the institution's credit extensions, applications and denials indicate that the institution is making the substantial portion of its credit available to all areas within its community. The institution has reviewed the geographic distribution of its credit extensions, applications and denials in a manner appropriate to the size and capacity of the institution and the nature and location of the community. Where that review has disclosed a very low level of applications from or loans to a particular neighborhood or area, especially low- or moderate-income areas, the institution has reviewed its marketing practices to determine what, if any, impact they may have had on the distribution. Where appropriate, the institution has either revised its marketing practices or lending policies or both. The institution's officers are reasonably accessible to all segments of its community and banking hours are tailored to meet the convenience and the needs of its customers. Finally, the institution considers, in advance, the potential impact of opening and closing offices on its ability to continue offering reasonably equal services throughout its community.

Rating Level 2 — The geographic distribution of the institution's credit extensions, applications and denials indicate that the lender is making credit available to all areas within its community. The institution has taken steps to eliminate unreasonable lending patterns disclosed by examiners or which have resulted from the review of the institution's policies or practices. The geographic distribution of applications reveals no pattern suggestive of any practice of discouraging or "prescreening" applications. The institution's record of opening and closing offices and the provision of services at its offices do not reflect any disparate treatment of minority or low- and moderate-income neighborhoods. Offices are reasonably accessible to all segments of its delineated community. Services and banking hours are periodically reviewed to assure accommodation of all segments of the delineated community.

Rating Level 3 — The geographic distribution of the institution's credit extensions, applications and denials may suggest unreasonable lending patterns. Management has not attempted to review its lending policies and procedures or to analyze the institution's lending patterns within its community. The institution's record of opening and closing offices and its provision for services at its offices may indicate a disparity of treatment between certain areas within its community. Such a disparity is isolated and not an overall intentional pattern or practice. Management has plans to undertake immediate steps to restore reasonably equal service to any affected areas.

Rating Level 4 — The geographic distribution of credit extensions, applications and denials reveal unreasonable lending patterns, particularly in low- and moderate-income neighborhoods or areas of racial/ethnic concentration. The geographic distribution of applications may indicate a possible pattern or practice of discouraging or illegally prescreening applications. The institution's record of opening and closing offices and the provisions of services at its offices may suggest a pattern of disparate treatment of minority or low- and moderate-income neighborhoods. The record might portray an institution that has systematically sought to close or curtail services at offices serving minority or less affluent neighborhoods while opening new offices in developing, majority or upper-income areas.

Rating Level 5 — The geographic distribution of credit extensions, applications and denials reveals extensive, systematic, and unreasonable lending patterns. The institution has adopted loan policies and procedures, such as unjustifiably high minimum mortgage amounts or down payments or restrictions based on the age of property, which have or can reasonably be expected to have a significantly adverse impact on loan availability in low- and moderate-income or minority neighborhoods. The institution's record of opening and closing offices and the provision of services at its offices suggest a continuing pattern of disparate treatment of minority or low- and moderate-income neighborhoods. Where this was previously cited, management has not taken any corrective action.

IV. Discrimination or Other Illegal Credit Practices (Assessment Factor (f))

The rating to be assigned here corresponds to the institution's composite compliance rating.

Rating Level 1 — The institution is in substantial compliance with antidiscrimination and other credit laws.

Rating Level 2 — The institution is in satisfactory compliance with antidiscrimination and other credit laws.

Rating Level 3 — The institution is in less than satisfactory compliance with antidiscrimination and other credit laws.

Rating Level 4 — The institution has an unsatisfactory record of compliance with antidiscrimination and other credit laws.

Rating Level 5 — The institution is in substantial noncompliance with antidiscrimination and other credit laws.

V. Community Development and Other Factors (Assessment Factors (h), (k) and (l))

Rating Level 1 — The institution has taken affirmative steps to become aware of the full range of community development and redevelopment programs within its community. It is actively participating in the development or implementation of such programs to an extent consistent with its size and capacity and the nature and location of the community. In non-MSAs, the institution has contacted appropriate government and non-government representatives to determine the level of community development needs in its area. It has then determined what areas are appropriate for its involvement and has initiated such involvement or has undertaken other types of activities not previously covered, which in the examiner's judgment reasonably bear upon the extent to which the institution is meeting the community credit needs.

Rating Level 2 — The institution is aware of community development/redevelopment programs within its community. It has advised appropriate community officials of its interest in participating in such programs and is already involved in some aspects of program planning or implementation. Or, the institution is planning to undertake a specific activity designed to help meet community credit needs, which has not been covered in other categories, within six months.

Rating Level 3 — The institution is only vaguely aware of the community development/redevelopment activities in its community. The institution has taken little affirmative action to become involved in community development or to learn the specific features of different programs. Management appears receptive to becoming involved or investing in one or more programs but prefers to wait for a request to be initiated by community officials. At such time, the institution will consider possible participation. Management has periodically discussed various efforts to respond to community credit needs but a specific plan has not been developed.

Rating Level 4 — Management is unaware of the existence or nature of community development programs within its community and has expressed no interest in pursuing this area. Management has not developed any other programs, which were not

covered previously, to help meet community credit needs. Management may be unaware of the CRA regulations' encouragement of institution involvement in community development/redevelopment programs.

Rating Level 5 — Management has repeatedly demonstrated its lack of interest in determining if community development projects exist in its community. It has not expressed an interest in developing its own response to community credit needs.

ATTACHMENT 3

SAMPLE FDIC SUPERVISORY ACTIONS RE: CRA

MEMORANDUM OF UNDERSTANDING

This Memorandum constitutes an Agreement between the and the Regional Director of the egional Office of the Federal Deposit Insurance Corporation. This Agreement is designed to address certain conditions disclosed in the Compliance Report prepared as of the close of business, , 1988, by Examiner

1. Within 60 days of the date of this Agreement, the Bank shall adopt a written Compliance Policy establishing its goals in the compliance area. This policy will provide for the appointment of a Compliance Officer and will set forth the duties and responsibilities of the Compliance Officer.

2. The Board and Bank Management shall provide continuing review over compliance matters and guidance to the Compliance Officer.

3.

4. Within 90 days of the date of this agreement, the Board shall reassess the Bank's CRA performance and make the operating and policy changes considered necessary to improve that performance, consistent with the safe and sound operation of the Bank. A written report of that reassessment should address each of the assessment factors outlined in Section 345.7 of the Federal Deposit Insurance Corporation's Rules and Regulations. That report should be submitted to the Regional Director.

5. The Bank shall provide the Compliance Officer with adequate time and training to become familiar with the various laws and regulations and to satisfactorily discharge his or her duties.

6. The Bank shall direct the Compliance Officer that within 120 days of the date of this Agreement, the Compliance Officer shall prepare a training program and participate in the training of other officers and employees on a continuing basis.

7. The Bank shall direct the Compliance Officer that within 120 days of the date of this Agreement, the Compliance Officer shall prepare a schedule of the continuing requirements of each regulation (type and timing of disclosures, approvals, etc.) so that all involved employees will be informed of the regulations requirements.

8. The Bank shall direct the Compliance Officer that within 120 days of the date of this Agreement, the Compliance Officer shall prepare written procedures for continuing follow-up and review to ensure that adopted policies are being followed on a consistent basis.

9. The Bank shall direct the Compliance Officer that within 60 days of the receipt of the Compliance Report, the Compliance Officer shall ensure corrective action has been taken on each type of violation reported by supervisory authorities, including each exception listed in the report, dated , 1988.

10. Within 90 days of the date of this Agreement, the Compliance Officer shall begin to make periodic reports to the Board on performance of the above duties and all other matters relating to compliance.

11.

It is agreed that within 60 days of the date of this agreement, the Bank shall furnish to the Regional Director a written report detailing the form and manner of the Bank's compliance with all of the foregoing provisions. Additional reports will be provided every 60 days thereafter until all the provisions of the Agreement have been met. This Agreement is effective upon acceptance by the Regional Director of the Region.

FEDERAL DEPOSIT INSURANCE CORPORATION

Accepted:

Regional Director

Date

Date

PURSUANT TO RESOLUTION ADOPTED BY BOARD OF DIRECTORS OF THE
IT'S DIRECTORS MEETING HELD
AT THE ON , 198

FEDERAL DEPOSIT INSURANCE CORPORATION
WASHINGTON, D. C.

In the Matter of	
	ORDER TO CEASE AND DESIST
	FDIC-
(INSURED STATE NONMEMBER BANK)	

("Bank"), having been advised of its right to a NOTICE OF CHARGES AND OF HEARING detailing alleged charges of unsafe or unsound banking practices and apparent violations of laws and regulations by the Bank and of its right to a hearing regarding such alleged charges under section 8(b)(1) of the Federal Deposit Insurance Act ("Act"), 12 U.S.C. § 1818(b)(1), and having waived those rights, entered into a STIPULATION AND CONSENT TO THE ISSUANCE OF AN ORDER TO CEASE AND DESIST ("CONSENT AGREEMENT") with a representative of the Legal Division of the Federal Deposit Insurance Corporation ("FDIC"), dated , 1988, whereby solely for the purpose of this proceeding and without admitting or denying the alleged charges of unsafe or unsound banking practices and apparent violations of applicable laws and regulations, the Bank consented to the issuance of an ORDER TO CEASE AND DESIST ("ORDER") by the FDIC.

The FDIC considered the matter and determined that it had reason to believe that the Bank had engaged in unsafe or unsound banking practices and committed violations of applicable laws and regulations.

The FDIC, therefore, accepted the CONSENT AGREEMENT and issued the following:

PAGES 2 THROUGH 6 DELETED

Examination Report; and (3) reporting at each Board meeting the results of such review procedures for inclusion in the minutes. Such monthly reports submitted by the compliance officer to the Board must include at a minimum: (1) each law or regulation reviewed; (2) details of exceptions noted; (3) any corrective action taken; (4) any training activity conducted during the period, indicating the subject matter and the names and job titles of employees in attendance; and (5) the compliance officer's opinion of the adequacy of the compliance operating procedures and the bank's current level of compliance.

LAST PAGE DELETED

7. As of the effective date of this ORDER, the Bank's Board of Directors shall require the designated compliance officer (1) to have continuous access to all prior and future FDIC Compliance Examination Reports and official correspondence relative to the Bank's compliance administration; and (2) to be provided with sufficient delegated authority, time and resources during normal working hours to study the Bank's previously adopted comprehensive compliance manual, update any obsolete material on an ongoing basis as necessary and, thereafter, strictly implement the provisions of the program contained therein.

8. Within 90 days from the effective date of this ORDER, the Bank shall take steps to improve its Community Reinvestment Act performance in a manner consistent with the recommendations set forth on pages 3 of the FDIC Report of Examination as of

--, 1987.

Original
Copy

MEMORANDUM OF UNDERSTANDING

This constitutes an Agreement between the board of directors of the , and the Regional Office of the Federal Deposit Insurance Corporation. This Agreement is designed to correct certain unsatisfactory conditions disclosed in the Compliance Report of Examination prepared as of the close of business , 1988, by Examiner .

It is agreed and understood that the board of directors shall, within 60 days of the date of this Agreement, take the following actions to improve the bank's compliance program:

1. Appoint a compliance officer to oversee and coordinate the bank's overall compliance efforts. The compliance officer shall be responsible for training and supervising all affected personnel in compliance related matters and shall be given necessary authority to implement appropriate compliance procedures. The compliance officer shall also be given sufficient time and resources to carry out his or her duties.

2. Ensure that the compliance officer receives necessary training as soon as possible after assuming his or her duties.

3. Adopt a compliance program that includes appropriate internal controls and training of personnel in all bank functions related to compliance.

4. Institute a review procedure whereby loan disclosure statements and adverse action notices are reviewed by a knowledgeable individual, other than the preparer.

With respect to the specific violations or exceptions disclosed in the Compliance Report of examination prepared as of the close of business 1988, it is agreed and understood that the board of directors shall, within 60 days of the date of this Agreement, take the following actions:

1. Establish and implement practices and procedures sufficient to reasonably assure compliance with the Truth in Lending disclosure requirements set forth in Regulation Z, and make efforts to avoid further violations of each type of Truth in Lending disclosure requirement, described in the Compliance Report.

2. Furnish a complete and accurate adverse action notice to applicants for credit as required in Section 202.9 of Regulation B, which implements the Equal Credit Opportunity Act.

3. Establish and implement practices and procedures necessary to comply with the provisions of Part 339 of the FDIC Rules and Regulations relating to loans in areas having special flood hazards.

4. Obtain, record and maintain the information on home loan applicants to the extent necessary to comply with provisions of Section 338.4 of the Fair Housing regulations.

5. Direct management to correct all other violations listed in the Compliance Report and institute appropriate procedures to prevent their reoccurrence.

In addition, the board of directors shall monitor and confirm the completion of actions taken by management to comply with the terms of this Agreement. The board shall so certify in writing to the Regional Director when the above actions have been accomplished. All actions taken by the board pursuant to this Agreement shall be duly noted in the minutes of its meetings. This Agreement is effective upon acceptance by the Regional Director of the Region.

DATED _____

_____
Regional Director
Federal Deposit Insurance Corporation

Comprising the Board of Directors
of

_____

_____

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Original
Copy

MEMORANDUM OF UNDERSTANDING

This constitutes an Agreement between the Board of Directors of the [ ], and the [ ] Regional Office of the Federal Deposit Insurance Corporation. In accordance with this Agreement, the bank will immediately undertake to, and, in no case later than 60 days from the date of this Agreement, take the following actions to improve the bank's compliance program:

1. Establish and implement practices and procedures sufficient to reasonably assure compliance with the Truth in Lending disclosure requirements set forth in Regulation Z, and make efforts to avoid further violations of each type of Truth in Lending disclosure requirement, described in the Compliance Report prepared at the , 1988 examination.

2. Establish and implement internal procedures to ensure compliance with Section 202.7(d) of Regulation B which implements the Equal Credit Opportunity Act.

3. Adhere to the provisions of the Community Reinvestment Act (CRA). Also, correct all violations of CRA described in the . , 1988 Compliance report.

4. Furnish the Good Faith Estimate and completed Uniform Settlement Statement (HUD-1) to the applicable borrower and/or seller as required by provisions of Sections 3500.7 and 3500.8, respectively, of Regulation X, which implements the Real Estate Settlement Procedures Act.

5. Correct all other violations listed in the Compliance Report of Examination and institute appropriate procedures to prevent their recurrence.

6. Appoint a compliance officer to oversee and coordinate the bank's overall compliance efforts. The compliance official shall be responsible for training and supervising all affected personnel in compliance related matters and shall be given necessary authority to implement appropriate compliance procedures. The compliance officer shall also be given sufficient time and resources to carry out his or her duties.

7. Ensure that the compliance officer receives necessary training as soon as possible after assuming his or her duties.

8. Adopt a written compliance program that includes appropriate internal controls and training of personnel in all bank functions related to compliance.

9. Institute a review procedure whereby loan disclosure statements and related documentation are reviewed by a knowledgeable individual, other than the preparer, prior to issuance.

In addition, the Board of Directors shall monitor and confirm the completion of actions taken by management to comply with the terms of this agreement. The Board shall so certify in writing to the Regional Director when the above actions have been accomplished. All actions taken by the Board pursuant to this agreement shall be duly noted in the minutes of its meetings. This agreement is effective upon acceptance by the Regional Director of , and shall remain in effect until terminated in writing by the Regional Director.

This Memorandum of Understanding shall remain in effect until terminated in writing by the Regional Director, or until the Regional Director shall receive written notice of rescission by unanimous action by the board of directors.

DATED Comprising the Board of Directors of

Federal Deposit Insurance Corporatio

Senator DIXON. Thank you very much, Ms. Smith.

LACK OF UNIFORMITY BETWEEN AGENCIES

One of the first things I would like to observe is that one of the complaints that we continuously receive in the committee is that there is a lack of uniformity to the method with which each of your four separate regulatory agencies does its job. I can't say that I get that sense as I hear your testimony. It doesn't sound all that different, the different things that you do.

But I would like to ask each of you how much communication is there between your agencies while you go about your business?

Mr. GARWOOD. Why don't I start?

It is just wrong to say that there is a complete lack of uniformity. Certainly, uniformity is one of our goals, and we have common examination standards, for example, that have been adopted by all the agencies.

I think it is fair to say that you will never have complete uniformity in every instance as long as you have four different agencies. Some variation is unavoidably just built into the system.

Certainly, we are always working against that and always very mindful of this criticism, particularly in cases where the Federal Reserve, for example, is acting on applications when the record in question is one of institutions supervised by a different regulator.

So it is something that we are very conscious of. We try to avoid it, but some variation probably is inevitable despite our best efforts.

Senator DIXON. Mr. Kluckman.

Mr. KLUCKMAN. I would like to add to that that there is a mechanism for exchange of information. That is the Financial Institutions Examination Council. There is a task force on consumer compliance. All five agencies, the four represented here plus the National Credit Union Administration, are represented. Janice, John, and myself are members of the task force, and we talk about things like this.

In addition, we established this past year a separate subcommittee to deal with nothing but CRA matters.

So there is a tension, and I have to agree with Mr. Garwood that we will never get complete uniformity, but I think there is a general tendency toward getting more uniform procedures.

As a matter of fact, our new program fairly closely resembles what the Federal Reserve is doing.

Senator DIXON. Mr. McDowell.

Mr. MCDOWELL. I would just echo Mr. Kluckman's comments. In addition to the CRA subcommittee, we have a HMDA subcommittee whose members are monthly and probably weekly talking with each other on issues that are coming out concerning the CRA and HMDA.

I believe the CRA is somewhat subjective. Examiners conduct these types of examinations with different banks, different backgrounds and in different kinds of cities. You are going to have an occasional difference.

Senator DIXON. Ms. Smith.

Ms. SMITH. Not much to add, but I believe that the task force has made an effort to come out with more uniform procedures, not just on CRA but all the consumer protection laws. We do have an examination procedure subcommittee, which we made a permanent subcommittee in recent months.

Also, perhaps the size of institutions, the type of business may also cause some differences. Smaller institutions might be looked at differently than the larger institutions.

Senator DIXON. I am interested in these observations about these committees on which you jointly serve. At least three of you have identified yourselves as being active on these committees—is that right—but obviously you all know one another, and it is quite obvious that you can communicate with one another and exchange your points of view.

Am I able to understand from this exchange that you all agree about the desirability of a degree of uniformity to the extent that that can be achieved in the four separate regulatory agencies?

Mr. GARWOOD. Yes.

Senator DIXON. In general, you would agree with that.

Are your folks, at least in your view, similarly trained in respect to what they are supposed to do when they go out to do these evaluations?

TRAINING PROGRAM

Ms. SMITH. I would say there is an effort to do this. I know in our case we are looking at developing more training, and part of that is more advanced training. We are actually taking a look at some of what the Federal Reserve is doing. They have an extensive training program.

I also had one of my staff members participate in the training program that the Bank Board has just begun to see what we might draw on from that.

Mr. GARWOOD. I can add that last week we had an examiners school at the Federal Reserve and half the students were from the Federal Home Loan Bank System. So there is a good deal of cross-training as well.

Senator DIXON. I like the thought of that. I think if you would attend these symposiums and conferences where you can share with one another these discussions, I believe that would be a valid thing.

Tell me, how exactly would an examiner conduct a CRA exam for you, Mr. Garwood.

Mr. GARWOOD. Well, we have specialized examiners, as I mentioned. They are not safety and soundness examiners. They are trained in all the consumer regulations. So they concentrate in that area, and they have the benefit of specialized training.

They would go into the institution. They would look at the loan policies and the employee training courses. They would look at the advertising materials that have been prepared. They examine the board of directors' minutes to see the extent to which the directors were involved in CRA matters. They look at the Home Mortgage Disclosure Act data, which plots the geographic location of home

loans, to see whether the pattern was appropriate or whether there was gerrymandering going on.

Senator DIXON. May I stop you at that point?

All of you check that question of geographic distribution of loans—do all of you do that?

Go ahead, Mr. Garwood.

Mr. GARWOOD. We would look at such issues, for example, as branch closings to determine whether, if branches have been closed, this was done with sensitivity about the effect it might have on the community and whether a firm financial analysis was done to support the closing.

We would look at the general volume of various kinds of loans and investments. Was there attention to the various kinds of CRA types of investments, for example? And then we would make outside contacts in the community with community groups, Government officials, with business people to try to develop our own sense of the credit needs of that community, against which then we could measure the performance of the financial institution.

Putting it all together, we would try to come to a judgment as to what the quality of their effort was and where we might advise them to do better.

Senator DIXON. Do you all check with community groups on a general basis, each of your separate regulatory agencies?

Mr. MCDOWELL. When we do our examinations, we don't routinely do so for the smaller banks. On the larger multinational banks we routinely meet with community groups every couple of years. We catch the other ones through our district offices. They have a program of outreach with the communities at the field office and district office levels.

Ms. SMITH. Our contacts with groups during an examination, I would say, are limited. We are trying to do more in this area. I do know that last fall during some of our compliance training sessions that we had here in Washington we began placing more emphasis on outside contracts as an important part of the examination process, and we are addressing outside contacts in training programs that we are developing. So there will be more outreach efforts in the future.

Senator DIXON. What would occur to us, quite obviously, on this side is that it would be important to always make inquiries of all the community groups to see whether you get some feedback because you could enlarge your scope of investigation, whatever community you are in, regarding whatever institution you are looking at. That would seem to be kind of an obvious thing to do.

Would you all agree with that?

Mr. MCDOWELL. I think the new statement that recently came out will encourage even more of that.

Senator DIXON. I think it was Mr. Kluckman who referred to the question of what might be occurring here, or perhaps it was Mr. McDowell.

Of course, we are all quite aware of the fact that there is an amendment in the thrift legislation that will shortly be before the two houses on the conference report. There are other matters that are more contentious at this point in time than CRA. But as I recall, basically, the Congressman Joe Kennedy amendment estab-

lishes four different ratings to be publicly disclosed: the first being an outstanding record of meeting community credit needs, the second being a satisfactory record, the third being a record that needs improvement, and the fourth being substantial noncompliance with community credit goals.

Now, when I did this first hearing as the Chairman of this subcommittee, pursuant to an agreement that we had reached with the Senator from Ohio, Senator Metzenbaum, during the original debate on the thrift legislation sometime ago—it seems like only yesterday, but it is a couple of months ago by now, isn't it—one of the really contentious issues was whether you would disclose the numerical ratings. The financial sector was concerned about that fearing that the ratings might appear to be a reflection on safety and soundness. I think that was largely their concern.

Would that be a fair, simplistic explanation of it?

Now, we have this nonnumerical rating system, don't we?

I would appreciate your views on that kind of public disclosure from the standpoint of the public's perception and of how useful it will be to advance CRA involvement in the communities.

Mr. GARWOOD. I think it would be very useful. We have supported the idea of giving the members of the community our assessment of the performance of institutions. We were very concerned about releasing numerical ratings. We were very pleased with that change in the language.

REPORT LANGUAGE

I would say with regard to that provision there is one area where we have some remaining concerns, and perhaps, Senator Dixon, you would have some influence along the way with the report language. We are anxious to have it made clear that we have the ability to speak confidentially to the institution in the areas that involve the privacy of their customers and individual employees, the institution's own financial condition, and other sensitive matters that we would want to bring to their attention to encourage good behavior. At the same time, we want to make full and fair disclosure of our overall assessment to the public.

Our sense is that it would simply set back the examination process to a certain extent if we could say nothing to the bank that we could not say publicly.

Senator DIXON. I will look at that, but I am told it is in the report language in that form.

Mr. Kluckman.

Mr. KLUCKMAN. We are pleased, too, that the bill would provide for adjective type ratings rather than numeric kinds of ratings. I think this is another opportunity for the agencies to work together because we are now going to be put in a position of forcing five ratings into four for public disclosure purposes. I think it is important when we do that to have something that is agreeable to all the agencies.

So I believe the Exam Council will be pressing this issue very shortly.

Senator DIXON. Mr. McDowell.

Mr. McDowell. I believe the adjective rating system that is being proposed is probably better for the local communities than giving them numbers. I think it will be more meaningful, as Mr. Kluckman said. It will be an improvement.

Ms. Smith. The same. We were opposed to the disclosure of the numerical ratings and feel that the adjective ratings will provide more information.

Senator Dixon. Now, I guess the quite obvious question that I would put to all of you at this point in time is, quite frankly, most people are disturbed by the very high number of 1 and 2 ratings, just a very, very high percentage, I think at one time above 98 percent. For the last year it is down to 93 percent for the Federal Reserve and OCC. I think most of us are concerned that there has been a disposition to be generous in these ratings.

First, how do you view that? What would be your response to that?

I heard your statement about people who have been involved in the community for a long time. Anyway, I am not terribly persuaded by that, but you are entitled to your point of view. But beyond that, what do you think about it from the standpoint now of these new requirements that you make public disclosures, at least indicating these four different criteria that I have set forth? Will there be an attempt on the part of the agencies to more carefully look at this in the broad view of the entire community?

Mr. Garwood. Let me speak about the current system just a minute and put it in perspective.

I think it is useful to have a full discussion of this issue because it is referred to in a shorthand way and has been described for a long time, in my sense, a little bit inaccurately.

Let me read you the second category, the "satisfactory" category. It simply says institutions—this is the description in our examination rating system—"institutions in this group have a satisfactory record of helping to meet the community credit needs. Institutions receiving this rating normally are ranked in the satisfactory levels of the five performance categories. Institutions in this category may require some encouragement to help the community credit needs."

In other words, this is not a high rating. This is saying it is satisfactory. They may need some additional encouragement.

So I think the characterization of 1 and 2 as high ratings is not quite accurate. In fact, it seems to me that 1 and 2 really are equivalent probably to A, B, and C in a regular grading system.

I don't know what the current grade distribution these days is in academic institutions, but I wouldn't be surprised if having 7 percent, for example, in the D and F category, which might be equivalent to our 3, 4, and 5, is a rather standard distribution of ratings.

So from that point of view, I wouldn't be so concerned by having 90-some percent in the 1 and 2 category.

Beyond that, the point I wanted to make in the statement was that there is a long legal tradition in this country calling on banks to serve the "convenience and needs" of their communities. It is in Federal law. It is in many State laws, and when CRA was first enacted in 1977, there were many people who thought that CRA was simply a confirmation of that existing legal principle.

So again it seems to me it shouldn't be surprising that you have pretty high numbers.

How this will match with the new system I am not sure because the C category in the new system is "needs improvement." As I mentioned, the existing number 2 category, the "satisfactory" category, today has the concept of still needing some improvement. So I think the Exam Council will just have to work through this as to how the new system will shake out.

Mr. KLUCKMAN. I am speculating that there probably will be some change in the actual ratings assigned as a result of the public disclosure. Typically, the ratings have been assigned as an internal supervisory item. A rating is given so the supervisors know what kind of action needs to be taken with an institution, and I think by making it public that you probably will see some changes in the rating distributions.

Senator DIXON. Mr. McDowell.

Mr. MCDOWELL. We are pretty comfortable with the rating distribution right now. I think the banks have done a pretty good job over the years. They are doing better and better. With our training of examiners, they have taken a closer look and ratings have dropped a little bit. I think there are around 10 percent unsatisfactory at this point.

Ms. SMITH. I think the FDIC is basically satisfied with our ratings. We find that our banks are generally in compliance with the CRA. We may see some changes as a result of the new system.

Senator DIXON. What geographic distribution of lending would present a problem, Mr. Garwood?

I am told that studies show three times as much lending in white middle class neighborhoods than in minority middle class neighborhoods.

Would that be the kind of thing that you would investigate? Would that get your attention?

Mr. GARWOOD. Yes, it would. In fact, those are the numbers that have been developed in Atlanta and in Detroit as well. We are doing a study in Boston right at the moment, and that is a very comprehensive study which should be released within the month. Those kinds of figures give you pause. They cause you to worry and to devote attention to the area.

ATLANTA INVESTIGATION

They do not answer the question of whether racial discrimination is occurring, however. There are lots of things at work; for example, the turnover of housing stock. In the Atlanta study the turnover of housing was about twice as great in the nonminority areas as in the minority areas. The value of the housing stock was about 25 percent less in the minority areas than it was in the nonminority. There were different preferences for FHA and VA loans, and those are offered more commonly by mortgage bankers than financial institutions that were active in the minority areas. And there were a variety of other factors. The banks may not have had the aggressive outreach that we would have wanted in those minority areas.

It is a complex set of factors that certainly merit concern, and the Department of Justice, for example, is now conducting an extensive investigation of the Atlanta situation.

Senator DIXON. Well, in a situation of that kind, as it comes to your attention, do each of your separate agencies go in there and ask penetrating questions and prepare reports to try to demonstrate in a meaningful way what the problems are and what can be done to alleviate those problems?

Mr. KLUCKMAN. Our examiners will be doing that. We have a system that is called the loan application register and data submission report system on which a number of these Atlanta Journal and Constitution articles were based. As part of our normal procedure, examiners will be going in and asking those questions. They will have that data available to them as part of their examination.

So I think the information there provides the direction as to what examiners ought to be looking at, yet they have to look at individual applications to make the determination of whether or not that loan application should have been rejected on the basis of economic standards or whether there was some discrimination and compare that particular applicant to other kinds of people in nonprotected classes who receive loans, for example.

Senator DIXON. How do you assign these CRA ratings; that is to say, after you have been out there and you get into the field and you have looked at all these records that you tell us you have looked at and talked to all the community groups, political leaders in the community, presumably movers and shakers of all economic types in the community, and so forth, and now you have this raw data, how do you assign the CRA rating ultimately to X institution?

Ms. Smith, how do you do it?

Ms. SMITH. We have examination procedures which include assessment factors and performance categories. Under each of those examiners look at the bank's outreach efforts in the community, the extent of their advertising and how they are determining credit needs. Examiners will tend to look at the different performance categories, try to determine the extent to which the bank is complying, and then it is their judgment as to how they weigh those as to what the rating will be.

JUDGMENT AND RECOMMENDATIONS

Senator DIXON. Who makes that judgment?

Ms. SMITH. The examiner.

Senator DIXON. The examiner in each individual case makes the judgment. Is there no overview of that? How many examiners do you have?

Ms. SMITH. We have about 2,000 examiners right now.

Senator DIXON. How many do you have, Mr. McDowell?

Mr. MCDOWELL. About 2,500.

Senator DIXON. How many do you have, Mr. Kluckman?

Mr. KLUCKMAN. We have about 1,600, but in the future only a small number of those will be making CRA evaluations.

Senator DIXON. For the purposes of this hearing, 6,600 so far.

Mr. Garwood?

Mr. GARWOOD. We have about 100 who devote themselves exclusively to consumer compliance matters.

Senator DIXON. Let me see if I get this straight. Is the ultimate judgment about the rating to be given to a named institution made at the examiner level?

Ms. SMITH. That examiner would make a recommendation.

Senator DIXON. Yes.

Ms. SMITH. And their examination report with the recommendation would go to the regional office. The regional office has staff which is dedicated to the compliance area, and they would review that. If they have questions, they would go back to the examiner, or perhaps to the institution, and raise further questions.

Certain things they can act on under delegated authority. Other matters must continue to come to Washington. We have Washington staff working in the compliance area who would review the reports and some cases actually have to go to our Board of Directors.

Senator DIXON. Roughly the same for you?

Mr. MCDOWELL. Basically, the same. The examiner makes the recommendation and forwards the report to the district or field office where the final decision will be made.

Senator DIXON. The same.

But there is some review of this, of the examiner's report and an evaluation made at a higher level, or higher authority. Then the decision is made there about how the rating is to be effectuated and applied.

Is that right in every case?

Mr. GARWOOD. That is correct.

Senator DIXON. Do you have any examples of supervisory actions that are taken outside the application process? How often do you do something like that?

Ms. SMITH. You mean where we have conditions to an application?

I would say that we have not had a nonprotested application that has CRA conditions.

Generally, when you are looking at an application, you have got a number of statutory factors to look at. One of those is convenience and needs, and CRA compliance is one of the components of those.

Senator DIXON. One of the things that—if I may interrupt—that we have observed is that unless there is some kind of a protest or action by some community group, I get the sense that nothing further is done.

Am I overcritical?

Mr. GARWOOD. Well, certainly the protests are the focus of lots of attention.

Senator DIXON. Obviously, when you get a protest it is going to come to your attention, and then you are going to do something about it. That is the usual human reaction.

What occurs to this Senator and some others who have suggested the same thing is that there must be plenty of times where you see this raw data and you see what the examiner has said and you think—you know, there must be plenty of times when it occurs to you that more ought to be done to ensure more community outreach by an institution.

What happens then? What do you do? Do you do anything?

Mr. GARWOOD. Our examination has two functions in this area, one to assess how well they are doing and, two, to encourage them to improve when they are not doing well. The examiners do that individually and then many times our community affairs specialists are called in to offer their services and advise banks on ways that they can do better in this area.

I might say as well that even in the case processing not all of what we think of as the CRA cases—those cases that involve major CRA issues—are cases that involve a protest. Last year, for example, looking at these CRA cases, we had 31 protested cases and we had 20 additional cases that we think of as ratings cases that rose to that level of attention simply because of a poor rating.

Senator DIXON. How many protested cases did you have?

Mr. GARWOOD. We had 31.

Senator DIXON. Out of how many cases all told?

Mr. GARWOOD. All told, about 2,000 each year. We had 2,128 last year, 31 protested cases, and then we had an additional 20 of these ratings cases that we think of——

Senator DIXON. May I interrupt at that point? When you say a protest case, you mean where a formal activity took place?

I would think it is not infrequent that you get a letter or two or some kind of a response suggesting that something is amiss that is not part of the examiner's report. Doesn't that happen?

Mr. GARWOOD. Not very frequently, really. During the course of examinations, as we call on our outside contacts, some of the groups would raise concerns about institutions. That happens. Then we have formal protests that are filed.

Senator DIXON. What happens when that is in the file?

Mr. GARWOOD. When that is in the file?

Senator DIXON. Let's take a hypothetical case of an institution that gets a favorable report from the examiner who says on the basis of his report he thinks that institution is a 1 or, at the very worst, a 2, and you see in there at the next level of evaluation that you have all described here a community action group that has indicated in the strongest possible terms another view. It might even be one of the classical institutional groups representing minority interests in the community or something of that sort that we would see there.

Is that any kind of a signal to you to make further inquiries before you come to the final decisionmaking process at the review level on the type of rating the institution would receive?

Mr. GARWOOD. I am not aware of that particular circumstance where you would have a good examination rating and then an outside group would step forward during the examination process, in essence, and raise those concerns with, in our case, the Reserve Bank before the examination is finalized.

There are cases in which we have had an acceptable examination and then during the course of the process of an application a group has stepped forward and raised concerns. Certainly in those cases, if we thought the examination had not looked into the area being raised in the protest, we would go back for an additional inquiry to see if we missed something.

Mr. KLUCKMAN. I believe if the examiner during an examination found in the comment file a letter from a particular group commenting upon the institution's CRA record, that the examiner would in the normal course contact that group and determine what the real concerns were. It would not be an appropriate examination to fail to contact someone who raised real concerns.

Senator DIXON. Well—well, go ahead, Mr. McDowell.

Mr. MCDOWELL. Our examiners do the same thing. If there is a letter of complaint in the public file, that would be followed up on in an examination. In addition to that, our examiners check our consumer complaint computer system for complaints concerning CRA filed against that particular bank, and they would be considered, too.

Senator DIXON. Well, you know, the obvious thing that occurs is that the approval rating is so high—we have discussed that previously—yet the continual complaints in the country at large about redlining and other practices is so prevalent that one wonders whether you are suggesting to me that this never shows up in the reports from your examiners.

I thought I heard there are 6,600 examiners out there in the country for the four regulatory agencies, and one is asked to believe that in a percentage in the very high 90's none of this ever seeps through from the examiners institutionally to the head people in the regulatory agencies.

Mr. MCDOWELL. We rarely get a complaint on CRA. I think last year we had zero and the year before that maybe three consumer complaints. As far as letters in the file, that is very unusual. We rarely find letters in the public file from consumer groups.

Ms. SMITH. The same here. We have received very few comments, but if a comment is received during the application process, we will in fact look into it. If warranted, it may be necessary to go into the institution to look into the matter. We have an obligation to satisfactorily resolve our convenience and needs factor before we act on an application. So we will take up any concerns that come up.

Senator DIXON. Would you all assert that your examiners are alerted to those kinds of concerns when they go into the separate communities?

I think you have all contended that you look at this geographic question, and so forth, and you do assert that you do do that, and your examiners are, you think, motivated to look for these concerns in their respective communities when they look at institutions?

Mr. GARWOOD. I think they are. I think one thing that may be very beneficial in this respect is the joint policy statement in which the agencies together have encouraged the institutions on an annual basis to be speaking more directly to the community about what their record has been. On the other side, the statement encourages people to step forward in connection with that annual statement and bring their concerns to the attention of the institutions and the examiners, therefore focusing some of the attention away from these relatively few protests back into the community on an ongoing basis.

Senator DIXON. Do any of you have anything further you would like to observe in connection with this before I conclude this hearing this afternoon?

[No response.]

Senator DIXON. I would before concluding simply make this final observation.

We want to hear from you—and we will develop a course of doing that in the future—about what happens in the event that the anticipated passage of the pending legislation takes place and these new public standards are placed upon you. Also, we will do some follow-up and would appreciate your being prepared for that in connection with joint efforts by all of your agencies to work together to continue to seek in every way possible uniformity of standards within and among the agencies—I appreciate the fact that it is four separate agencies—that will permit us to assume that you are making every effort out there to do that sort of thing on an ongoing basis.

I thank you all for taking the time from your obligations this afternoon to accommodate the committee. Thank you very much.

[Whereupon, at 3:10 p.m., the subcommittee was adjourned.]

[Responses to written questions of Senator Dixon from Griffith L. Garwood, Jerauld C. Kluckman, John H. McDowell, and Janice M. Smith follow.]

Questions for the record for the Federal Reserve Board from Senator Dixon from the July 31, 1989 hearing

Questions and Answers

1. How specifically is an institution to ascertain the credit needs of low- and moderate-income neighborhoods? How specifically will an examiner determine whether an institution has fulfilled this obligation?

Institutions may ascertain the credit needs of their communities in a variety of ways, such as through regular contact with customers, meetings with community groups, marketing surveys or studies, Board of Director memberships or directorships in economic development or other organizations, and discussions with elected officials and government agencies. Some of these are described in the Joint Policy Statement on CRA issued by the federal financial regulatory agencies in March. How examiners determine the extent to which institutions have ascertained local credit needs is addressed on pages II.1.48 and 49 of the uniform interagency examination procedures for CRA, a copy of which is attached.

2. Would marketing only to high income areas and not to moderate-income areas be non-compliance with the CRA? What sort of marketing is required?

No specific type of marketing is required by the statute or the regulation, but institutions are generally expected to make their credit services available in a non-discriminatory manner, throughout their delineated community. The kinds of marketing and outreach which we take particular note of in evaluating CRA performance are described on pages 5 and 6 of my testimony.

In our view the CRA does not prohibit an institution from offering certain products geared to high income clientele, or from directing its marketing of those products to that audience--as long as the totality of its services help to meet the credit needs of its entire community, including low- and moderate-income areas. There may be situations, however, in which a bank's delineated community has no low- and moderate-income areas, for example, a small bank located in the suburbs. Assuming that the bank's community delineation does not unreasonably exclude any such areas, the bank would be doing what is expected by CRA by serving its own community. The examiner would not be precluded from assigning a satisfactory rating even if there was no marketing to low- or moderate-income areas (assuming there were none within the designated community.) The statute directs us to assess a state member bank's record of "meeting the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with the safe and sound operation of such institution." If there are no low- and moderate-income areas in the community and the bank is serving its entire community, then it is doing what is expected. Obviously, care must be taken in deciding that such a delineation is, in fact, reasonable.

The answer to your question is clearly more complex when dealing with a bank with low- and moderate-income areas in its immediate vicinity. Assuming that there are both low- and moderate-income areas and more affluent areas in a bank's delineated community, a satisfactory rating would not be given if the bank is not taking steps to serve all parts of that community. It may choose to serve the various parts differently by offering products that meet the different needs of the various areas, if that is appropriate. It might also, for example, specialize in serving a higher income clientele in its retail strategy but conclude that it can best meet the needs of the low- and moderate-income areas by investing in local bonds, assisting minority enterprises, participating in public/private partnerships for commercial revitalization and low- and moderate-income housing and the like. Furthermore, it may use different forms of outreach and advertising to get its product offerings before the various parts of its market in the way that is most effective.

It is difficult to come to a single simple answer to is question because all banks are different and they serve different communities with different characteristics.

I want to be clear, however, that a state member bank that unreasonably excludes low- and moderate-income areas from its delineated community, or fails to help serve the needs of those that are in its delineated community, is unlikely to get a satisfactory rating from our examiners.

3. How specifically do you analyze the geographic distribution of credit? How exactly is the HMDA data used? What would be an acceptable geographic distribution? What would be unsatisfactory? Provide several examples.

Pages II.1.50 and 51 of the uniform interagency CRA examination procedures describe how the geographic distribution of credit is analyzed. These procedures are part of the larger focus on detecting illegal credit discrimination which, in addition to an analysis of where loans are actually made, also includes a review of the bank's lending policies and practices to see that they do not discourage loan applications, a review of the distribution of applications and denials, and compliance with consumer credit laws more generally. In this context, examiners compare key "profile" information from both accepted and rejected loan applicants, looking for any differences in the way the institution's stated lending standards have been applied. Loans may also be geocoded, or plotted on a map by census tract, which readily indicates whether lending has failed to reach specific areas.

HMDA data reported by institutions is compiled and matched against census data. It is then made available to regulators (and to the public at central repositories within each MSA) in the form of tables which present breakdowns of lending by

individual institutions, and by aggregate lenders within each MSA, according to location, age of housing stock, income level and racial characteristics.

There is no "acceptable" or "unacceptable" distribution of loans that applies to all cases. This is particularly true given the importance demand and competitive factors play in determining where, and in what volume, loans are extended. However, for purposes of analysis, we have found it helpful to compare the percent of mortgage and/or home improvement loans made by a given lender in low- and moderate-income neighborhoods, with the percent of loans made in those neighborhoods by all reporting lenders. We have also found it helpful, when comparing lending patterns in different census tracts, to calculate the number of loans made per owner-occupied unit, given that disparities may sometimes be due to a high incidence of rental housing.

Attached are redacted examples of the analysis performed of HMDA lending patterns in several application cases in 1989.

4. How many applications have been approved without conditions when the financial institution has had a less than satisfactory rating?

Between 1983 and 1988, the Board approved about 70 applications where a CRA rating was less than satisfactory--and very few of these involved a CRA protest. To put this in perspective, those 70 applications represent less than 1 percent of the total number of bank holding company applications handled by the Board during those years.

The Federal Reserve has seldom used conditional approvals in applications raising CRA issues, although it does make use of approvals with commitments. In all these cases where an institution party to the application has had a less than satisfactory rating, the applicant must have already taken corrective action to address any CRA deficiencies, or must have made commitments to do so, before processing of the proposal is completed. In this respect, we operate like we do when improvements have been needed in such matters as financial or managerial weakness.

5. The March Joint Statement by the Exam Council encourages a dialogue between banks/thrifts and community groups through the expanded CRA Statement and public comments thereon. Do you yet know how many banks and thrifts are now writing expanded CRA statements and how many are getting comments from community groups?

We do not have any statistical information in that regard at this point in time. We have talked informally with bankers, and have been told by many that they are in the process of acting on

the Statements guidance and recommendations. Our examiners conduct CRA examinations in light of the Joint Policy Statement, noting the specific measures taken by a bank in response to the Statement in their findings, as appropriate.

6. Describe how and when examiners contact community groups during an exam. How do examiners decide whom to contact? In what percent of exams are community groups interviewed? What are they asked?

As a matter of long-standing policy, our examiners conduct interviews with people outside of the bank during the course of each CRA examination. These contacts include consumer advocacy groups, housing coalitions, local business and trade associations, and government officials and other sources of information about the communities' credit needs. Since all of these organizations are outside the bank they might all be considered "community groups" in a broad sense. If so, such contacts are made in one hundred percent of the examinations.

In some small rural communities there may be no organized "community groups" of the more limited type one traditionally thinks of in an urban setting. Consequently, if that is the definition used, such contacts would be made in something less than all of the examinations. We do not, however, have data that would provide an exact percentage; but, it is our policy in all cases to encourage examiners to seek out the best community input possible to help make an honest assessment of the bank's CRA performance.

These contacts are selected by examiners in a number of ways. Frequently examiners telephone local housing departments or agencies to identify contacts, and to ask for referrals. Community Affairs Officers at the Reserve Banks provide ideas to examiners for contacts and conduct many such contacts themselves. Reviewing the bank's CRA public file and previous CRA examination reports can yield possible contacts. If there has been recent CRA-related dialogue or protest activity in or near the bank's service area, those protestant organizations or individuals involved may be contacted.

Points to be covered in the interview are the contact's perceptions of how the community may grow and prosper; what types of credit would assist in the community's improvement, whether they are currently available, and from whom; how specific financial institutions are involved in the community; what areas of the community are most in need of help; whether there are additional programs financial institutions could utilize to further satisfy the community's credit and service needs; and whether there is any indication that any protected classes (which are articulated in the Equal Credit Opportunity Act) have experienced discriminatory practices by financial institutions. The form our examiners use for recording community contact interviews is attached.

7. When the Federal Reserve Board reviews an application on CRA grounds, its order on the application routinely includes a discussion of the issues raised, the Board's assessment of the bank's performance with respect to those issues, and how its conclusions affected the final decision. This type of discussion has proved helpful - to lenders and community groups alike -- in providing insight into the Board's interpretation of CRA. Are the other regulatory agencies willing to follow this practice?

This question is not applicable to the Federal Reserve.

8. Since there are no performance standards for measuring CRA performance and assigning ratings, what assurance is there that ratings are assigned consistently by different examiners, within different regions of each agency, and across agencies?

On the contrary, there are definite standards for measuring CRA performance and assigning ratings. These are set out in the twelve assessment factors contained in Regulation BB and in the uniform interagency CRA ratings system, copies of which have previously been provided to the Subcommittee and which are attached hereto. As I indicated to you on page 7 of my testimony, these standards are generally qualitative rather than quantitative in nature, describing the type rather than the specific amount of activities institutions should be engaged in to merit ratings on a 1 to 5 scale. They acknowledge that financial condition and size of the bank, the urban or rural character of its locale, the competitive environment and the prevailing local economy will have a significant impact on how CRA obligations are addressed.

To ensure consistency within the Federal Reserve System, we review examination reports on a sample basis here in Washington to ensure policy is adhered to in citing violations and assigning ratings. With regard to the four regulatory agencies, substantively similar implementing regulations for the CRA have been adopted, and a uniform rating system is followed.

At the same time, I would frankly say that assessing CRA performance inherently involves a measure of subjectivity, as well as the examiner's professional judgment and insight; it cannot be reduced to a mechanical, lockstep process. We do our best to ensure uniformity through examiner training and review of examination reports. We also address general questions relating to CRA examinations through the Federal Financial Institutions Examination Council; for example, the Council has issued a "Question and Answer" document on CRA issues which have arisen, primarily as a result of field experience.

9. Do financial institutions derive any benefits for achieving a top CRA rating? Should they? What specific recommendations would you have?

Institutions do derive benefits, in the sense that their economic success is very much linked to the growth and prosperity of their communities--which they can promote through their CRA efforts. We believe institutions should comply with the CRA because it is the law, and would not be in favor of any kind of special rewards to those which fulfill their legal obligations. Some of the proposals I have heard discussed in this regard--such as paying interest on required reserves for high-rated institutions--have severe problems.

10. Some banks claim that their CRA ratings have been downgraded because of agency criticism of their documentation. This apparently occurred even when the bank in question was performing on CRA in a superlative manner. How much new emphasis is being placed on CRA documentation as opposed to performance? How do you balance the two?

The CRA Policy Statement affirms that the agencies expect financial institutions to manage their CRA responsibilities like they do other aspects of their business. One element of good management, typically, is reasonable documentation. While not intended to require documentation simply for the sake of documentation, the Policy Statement does explain that such documentation will be a key factor in the agencies' ability to analyze the issues in a CRA-protested application quickly and thoroughly. We have also conveyed in the Policy Statement that we are endeavoring to shift our focus to the examination as the gauge of how well a bank is performing under the CRA, and away from the highly pressured application process. Consequently, it is very much in a bank's interest to keep good documentation of its CRA activities to "answer" a CRA protest, to present during a CRA examination and, just as importantly, to facilitate its own self-evaluation of its own performance as a part of its effort to manage this responsibility.

Nevertheless, while we have urged banking organizations to document their efforts for these reasons, I would not say that we have placed any "new emphasis" on documentation with respect to the assignment of ratings. In fact, I am not aware of any state member bank whose CRA rating has been downgraded simply because of poor documentation. A deterioration in the rating is apt to be evidenced if the institution has done little to manage and document its own performance, thereby indicating it has no process in place for dealing with CRA. However, this certainly would not be the case if the performance has nonetheless been demonstrably satisfactory.

11. Do agency procedures require examiners to review existing CRA agreements between lending institutions and community groups. If so, describe the procedures. Do examiners routinely assess a financial institution's implementation of such an agreement in evaluating an institution's CRA performance? Do the procedures require examiners to contact the community groups as part of this

evaluation?

It is the Board's policy to encourage banks and community groups to talk with each other and, as much as possible, to resolve their differences. However, it very firmly believes that any agreements made by banks with community groups are private matters which it does not enforce. Therefore, examination procedures do not call for the examiner to make sure they have been complied with. In this respect, they are unlike commitments made by banking organizations to the Board, which definitely are subject to supervisory follow-up. This distinction is important because many of these private agreements contain specific lending targets or other provisions which could bring the Board into the business of allocating credit or "favoring" one particular community group over other equally worthy ones.

At the same time, I should point out that in many cases the private agreements do result in special initiatives by a bank to improve its community outreach, its lending, or other credit-related services. Such initiatives may very well strengthen bank performance in one or more of the CRA performance categories and would, naturally, be reflected in the examiner's assessment of the bank's record. This record would not be reviewed, therefore, in the context of enforcing the agreement but, rather, of assuring that a complete and accurate assessment of that record is reflected in the examination report and the rating assigned.

As mentioned under question 6, examiners may interview a community group which has entered into a private agreement with the bank being examined as one of their routine "community contacts," although examination procedures do not require them to contact that particular group. Other organizations, businesses, agencies or individuals may have an equal or superior claim to the examiner's attention in that community.

12. All of the agencies indicate that HMDA data is integral to CRA evaluations and helps them to determine the degree to which lenders are serving various parts of their communities with respect to mortgage loans. Would comparable data for commercial lending be equally useful? If not, why not?

No, I do not think so. First, unlike with HMDA, such data would not be very reliable as a geographic indicator of the impact of the credit extension. For example, a business loan may not be used in the same neighborhood, or even the same city, where the business that took out the loan is located. It would also be difficult from a reporting standpoint, since such diverse arrangements as overdraft privileges, credit card accounts, accounts receivable financing, revolving lines of credit, various lease financing, mortgage loans as well as working capital loans can fall into the "business loan" category. Sorting out the varying impacts of all these kinds of loans, determining their geographic importance and coming to a reasonable CRA assessment

in an examination report would be extremely difficult and of questionable value. It would also be very expensive for the regulators and the industry, and I question whether the expense would be worth the results that could be achieved.

We have found that knowing on a more "micro" basis the number and kinds of business loans a bank provides, the terms under which such credit is extended, and the location of the businesses involved often tells us more about how well it is serving the needs of the business community than a "macro" data bank showing the distribution of all such loans. For example, we are interested in whether the bank has participated in government-insured, guaranteed, or subsidized loan programs, such as the SBA programs and similar state or locally-sponsored programs. We check to see whether efforts have been made to tell local businesses, including those which are minority or women-owned, about the institution's services. In an urban setting, we would also consider favorably a bank's support for a Minority Enterprise Small Business Investment Corporation (MESBIC) or Small Business Investment Corporation (SBIC). In all of this, however, our examiners would be able to look beyond the raw data to the purpose of the loan to more accurately judge its impact on the bank's community. We think this more "micro" data about the individual bank being reviewed is sufficient to our purpose and more valuable than the "macro" data that would be gleaned from a HMDA-type system for all commercial loans.

13. A recently released study by the Center for Community Change found that banks and thrifts lend, on average, 3 times as much in white middle class neighborhoods than in minority middle class neighborhoods. Why does this sort of redlining still exist? Should not enforcement of CRA laws stop redlining?

I have not seen the study by the Center for Community Change, although I am familiar with studies published in Atlanta and Detroit newspapers which had similar findings. Those studies are correct in pointing out that more home purchase loans were extended in mostly white neighborhoods than in mostly minority areas with roughly the same income. However, none of those studies could clearly conclude that the lending disparities resulted from illegal discrimination by lenders. Other possible explanations are also plausible, such as the influence of other factors in the market, like the real estate brokers and appraisers, a failure by lenders to adequately market their lending services in those areas, and factors relating to the demand for credit. Though discrimination is a possible cause for the disparities, it is not prudent to conclude from the studies done to date that that is the cause without a doubt.

The conclusion that racial discrimination is the cause for the disparities cited by the various studies is seriously questioned by their failure to take into account home improvement loan activity, which is a significant aspect of housing-related credit--and is often especially needed in those low- and

moderate-income areas with older housing stock. The studies either omit mention of, or give little credence to, the fact that loans to those same minority neighborhoods for home improvement outnumbered home improvement loans to their mostly white counterparts. If lending patterns were the result of racial redlining, why would this be the case?

These studies raise very serious issues, which the Federal Reserve, along with others, is seeking to address. Yet I do not think we can conclude, as your question implies, that commercial banks and thrifts are guilty of racial redlining without a more thorough analysis of all the factors at work--including the frequency of housing turnover in the respective neighborhoods, the loan activity of mortgage bankers, and the differences in loan products offered by commercial banks and other lenders, and factors other than income that affect creditworthiness. There are deeply rooted historical preferences involved--including, in some cases, an outright distrust of banks and reluctance to deal with them - that we need to try to understand if we are to overcome it.

With regard to our enforcement of the CRA, trying to prove that racial discrimination has taken place is a difficult, frequently inconclusive job, given that such a conclusion should not be reached lightly and should be supported by evidence showing that persons similarly qualified for purposes of creditworthiness were treated differently, solely because of their race or other protected characteristic. Nevertheless, our examinations do reveal CRA deficiencies--such as the failure to effectively market services in minority communities, or the existence of underwriting criteria which make it more difficult for minority applicants to qualify for credit--which contribute to racial disparities in lending. We point these out, and work with institutions to correct them. But our efforts to enforce the CRA, the Equal Credit Opportunity Act and the Fair Housing Act, though conscientious, may not be able to eliminate factors at work that may go well beyond the particular bank being examined or the banking system as a whole.

14. Each agency's testimony provided data on how many hours examiners spend per CRA exam. Clarify your methodology, as it is uncertain whether each agency followed the same methodology in calculating the hours.

Attachment E to my testimony (copy attached) provides the number of hours spent per examination, indicated according to bank asset size. The number of hours included time spent conducting the examination on bank premises, conducting community contact interviews at various locations in the community, and preparing for the examination in the Reserve Bank--usually in analyzing HMDA data and reviewing previous examination reports as well as demographic or other information about the bank's community.

15. Page five of the Federal Reservé's testimony describes the types of information reviewed in assessing the marketing and special credit programs assessment factor. At the selection of the the Federal Reserve, about a dozen CRA exams were provided to the Subcommittee staff. Those selected reports had scant evidence of any special focus on the low and moderate income neighborhoods in marketing efforts. What explains this seeming contrast between your testimony and the apparent implementation of policy?

I do not believe the examination reports show any such contrast. At the Subcommittee's request, our selection included some reports for other than "good" performers where such targeted marketing efforts were absent. Other reports dealt with banks in communities--notably, those in rural settings--which are largely homogeneous; I think the reports made this situation clear.

Under the performance category "Community Credit Needs and Marketing," the reports describe, where applicable, specific marketing and advertising efforts aimed at low- and moderate-income segments of the community. Other reports discuss outreach efforts more generally, such as contacts with realtors, community breakfasts hosted by a bank branch in a high minority neighborhood, officer call programs and many other activities which open the lines of communication between a bank and the people it serves. Because each bank and its community is different, the degree to which marketing efforts are targeted to lower income areas varies accordingly--and this is appropriately reflected in reports of examination.

16. According to your testimony, the Federal Reserve monitors CRA compliance with follow-up correspondence and visits. In what percentage of cases does this occur? Are there other sorts of supervisory actions which the Federal Reserve has taken? Under what conditions and in what percentage of cases?

The CRA statute does not authorize us to engage in formal supervisory actions, such as Written Agreements or Cease and Desist Orders. Our mandate under the law is to encourage banks to help address local credit needs throughout their entire community, and we certainly attempt to do so with our examination program and through our Community Affairs Program, which has conducted a great deal of outreach, held hundreds of educational conferences, and produced a wealth of written information on community development lending techniques and opportunities. The statute also calls upon the Board to take the applicant bank's CRA record into account when considering applications for merger, acquisition, branching, or forming a holding company - and this does give us a significant lever for ensuring that banks have satisfactory records.

As I mentioned in my testimony, we are rigorous in examination follow-up in those cases where bank performance is unsatisfactory. The Reserve Banks are responsible for providing

the supervisory attention needed to assist state member banks with identified CRA weaknesses in improving their performance. As part of their routine examination followup--for all examinations conducted regardless of the rating assigned--Reserve Banks expect bank management to provide a written response to any serious adverse CRA findings. If a bank's response fails to address examination criticisms in a satisfactory manner, the Reserve Bank pursues the matter in further correspondence and meetings with management and boards of directors and through follow-up examinations. We do not maintain figures on the percentage of cases in which this occurs. Of course, examiners also always check to see that corrective measures have been taken at the next examination.

Under the Board's examination frequency guidelines, banks exhibiting significant CRA weaknesses are, by virtue of their adverse rating, required to be re-examined within 12 months (in the case of 3-rated banks) or within 6 months (in the case of 4 and 5-rated banks), rather than according to the standard 18 month interval. In 1988, and as of the third quarter 1989, 7 percent of state member banks were assigned ratings of 3, 4 or 5, and therefore were subject to the more frequent examinations.

Assistance provided by Community Affairs Officers to state member banks, bank holding companies, and others in developing a satisfactory record is also provided at the institution's request--most often on referral by examiners who have identified CRA weaknesses. We have no precise figures on what percentage of state member banks have accepted CAO assistance, but we do know that our CAO's have helped scores of banks--not limited to state members--in this manner.

17. In approximately one third of the Federal Reserve's protested cases CRA commitments are made. This is a significant percentage. What happens in non-protested cases?

My testimony explained in pages 11-14 that CRA performance is one of the statutory factors the Board must consider in its review of certain applications. The CRA merits of the case are subject to careful review, particularly when a protest has been filed or when any of the banks party to the application have been assigned an adverse CRA rating.

In some of these cases we find that corrective measures have already been taken to address the weaknesses identified during the examination, and the institution is able to demonstrate to us that current performance is satisfactory. In other cases, commitments have been made to correct the deficiencies. The Board and other financial regulatory agencies have believed that using commitments to improve the bank's record was appropriate, constructive, and consistent with what was done when other aspects of an applicants record needed improvement.

However, that approach has changed somewhat under the interagency CRA Policy Statement issued in March. Under that statement, where the overall record of an applicant is satisfactory but some specific weaknesses are evidenced (where, for example, only one out of several subsidiaries of an applicant holding company has a less then satisfactory rating), commitments may be offered to enhance performance before processing of the application is completed. The March Policy Statement clarifies the agencies' expectation that applicants will come to them with a sound program and a good record already in place. The important thing to note is that, in all cases where any CRA weaknesses are evidenced, the weaknesses have been fully addressed through commitments or through corrective action already implemented before processing is completed.

In 1988, the Board staff handled 20 cases with adverse CRA ratings where there was no public protest. Commitments for improved performance were made in 7, or 35 percent of those cases. In 2 instances, applications were withdrawn by the applicant, it having been advised by Board staff that CRA deficiencies posed problems in processing the case. In one other case, the processing of the application was suspended. Ten ratings cases were approved without commitments; in 9 of those, the applicant institutions had already taken action to correct deficiencies and had satisfied their primary regulatory agency that the action taken was appropriate. In one case, the institution's written response to examination criticisms, indicating the corrective action to be taken, was deemed adequate in lieu of formal commitments.

In 1989 the adverse ratings cases which involved no protest increased to 42. In 10, or 24 percent of those cases, commitments were made, and 5 applications were withdrawn. Nineteen cases were approved without commitments. In 11 of those cases, corrective action had already been taken by the applicant institutions; in 5 cases, deficiencies were confined to the target institutions, and would be corrected by the applicant (having a demonstrated satisfactory record) after consummation; in one case, the institution had recently come under new management and steps were being taken to improve CRA performance. Two cases involved notifications of change in control where CRA performance is not explicitly one of the factors the Board is obliged by statute to take into account, but is considered to have a bearing on the overall competence of management. In one change of control case, a determination was made that an adverse rating, assigned on a preliminary basis to an institution affiliated with the applicant (but not directly party to the application), did not affect processing of the case; in the other instance CRA performance was deemed to reflect negatively on the institution's record but did not outweigh other financial, managerial and legal considerations. Eight adverse ratings cases are pending as of this date.

18. Under what conditions will the Federal Reserve order a new CRA examination when an application is being considered, instead of deferring to the institution's usual examining agency? How often does this occur and what have been the results of these new examinations?

Our practice is to request the institution's primary regulator to provide the information needed to construct a complete, accurate profile of the institution's record when CRA issues are presented by an application. We have no authority, however, to order another agency to conduct an examination, nor do we make sending one of our examiners into a bank a matter of routine practice. Doing so would raise a number of very problematic issues. However, in cases where examination findings are outdated our request may lead to a new examination by the primary regulator. We may also find that a new CRA examination is already in progress, or that the primary regulator intends to begin one shortly when we are performing our analysis of CRA issues. In these cases, we generally wait to receive the results of the new examination before going forward with our analysis.

New examinations were conducted in 6, or 19 percent of the 31 CRA-protested applications handled in 1988, and in 4, or 25 percent of the 16 such cases handled in 1989. In 1988, 1 new examination was conducted in an adverse ratings case, representing 5 percent of those cases. In 1989, new examinations were conducted in 9, or 23 percent of these cases. In some of these cases, generally because other agencies were involved, it is not clear whether the examination was actually triggered by the pending application, or whether it simply coincided with the application on the normal frequency schedule.

Obviously, the results of each of these new examinations are unique. In general, the examination findings either reveal that allegations put forward by a CRA protestant are unfounded, or suggest that weaknesses do exist in the record - whether or not they coincide with the protest's concerns. Where an adverse rating is at issue, they tell us whether deficiencies noted at the last examination have been addressed and a satisfactory rating is now warranted.

We consider examination results to be singularly important, and generally we have no reason to disagree with the primary regulator's rating and assessment. However, the Board must, and does, render its own decision on the applications that come before it and on rare occasions has come to a different result than the primary regulator after its own review.

19. In 1985 and 1986 99% of banks received satisfactory ratings. In 1988 and so far this year, only 93% have. Did banks change or did the Federal Reserve?

First, bank membership in the Federal Reserve is not static--each year, we gain some state member banks and lose others

through merger, acquisition, or simply withdrawal from the System. Since the set of banks we examined in 1985 and 1986 is not the same one we are examining this year, some difference in the ratings might be expected.

Second, I would say that the agencies' examiners have improved with experience and training, and our expectations regarding what constitutes a satisfactory record would naturally increase with time and experience by banks in dealing with their responsibilities. If we were to expect in 1988 and 1989 only what was forthcoming earlier in the decade, then no progress would have been made. We have worked to enhance the CRA training given to our examiners, and I am sure we have managed to convey a sense of concern for thorough, insightful examination findings, especially in light of the policy directions in the interagency CRA Policy Statement. Given these factors, I am not surprised to see something of a decline in the ratings.

20. In certain cases the Federal Reserve Board has required CRA commitments from bank holding companies as part of application approvals, or parent companies have reached CRA settlement agreements with protesting community groups. Frequently, these commitments must be implemented in part by the companies' bank subsidiaries, which are supervised by other regulatory agencies. What procedures does the Federal Reserve have for monitoring the implementation of these commitments and/or informing appropriate regulatory agencies about them?

As explained in my answer to question 11, private agreements are quite different than commitments made to the Board, and are not enforced - for good reason - by the Federal Reserve.

Commitments made to the Board are, however, subject to System monitoring. The method of monitoring will vary depending on the type and number of commitments made, and the experience the Board has had in dealing with that applicant in the past. It may be appropriate in some cases to simply ask for a one-time report from the company, await a further application, or require periodic reports to the Reserve Bank, depending on the circumstances.

In many of the cases where commitments are made, the Board has required annual, semiannual, or quarterly reports to the Reserve Bank, which reviews them for completeness and adequacy. These provisions are specifically laid out in the Board's order containing its decision. Where the banks are state members of the Federal Reserve System, compliance would also be verified in conjunction with regular consumer affairs/CRA examinations by the Reserve Bank. We do not have a specific mechanism for informing the other agencies, although they will generally know of Board orders affecting their institutions. Perhaps this is an area that could be improved, however.

21. Page nine of the Consumer Bankers Association's testimony describes how S. 909 could be interpreted to require banks to comply with each of the twelve assessment factors. Does the Federal Reserve Board expect compliance with all twelve of the assessment factors?

Yes, but in a limited sense. As made clear in the uniform interagency CRA rating system (copy attached), CRA examiners rate performance in five performance categories -- Community Credit Needs and Marketing, Types of Credit Offered and Extended, Geographic Distribution, Discrimination or Other Illegal Credit Practices, and,Community Development and Other Factors -- which represent groupings of all twelve assessment factors set out in the regulation implementing the CRA. Thus all twelve factors are reviewed.

Yet it is not really correct to say that we expect banks to "comply" with each of them. Each assessment factor is reviewed and taken into account under one of the five performance categories, but we do expect that banks will exhibit varying levels of activity under the factors for reasons that reflect the credit needs of its community, or the bank's expertise and business orientation.

For example, a bank may choose not to participate in governmentally-insured, guaranteed, or subsidized loan programs for housing, small business, or small farms, even though participation in such programs would be considered under the tenth assessment factor which calls for the review of these activities. Examiners may conclude, in light of the bank's performance under the other assessment factors that are weighed in this category, that the bank is doing a satisfactory or even outstanding job under the category. This would be the case if, for example, examiners found that the bank lacked the expertise to participate in such programs, or that the bank's efforts to ascertain local credit needs revealed that a need for federally-assisted mortgage credit simply did not exist in the community, or was already fully addressed by other institutions. Examiners might also have found that the range of conventional loan products offered by the bank was on target in responding to local needs for credit. The point is that examiners focus on the totality of efforts made within each grouping of factors that constitute the performance categories, rather than on single factors independent of each other.

Office of Thrift Supervision
Department of the Treasury
801 Seventeenth Street, N.W.
Washington, D.C. 20006

September 26, 1989
(Corrected)

The Honorable Alan J. Dixon
Chairman, Subcommittee on Consumer
and Regulatory Affairs
Committee on Banking, Housing and
Urban Affairs
United States Senate
Washington, D.C. 20510-6075

Dear Senator Dixon:

Thank you for your recent letter requesting additional information for the record relative to the Community Reinvestment Act testimony I delivered before the Subcommittee on July 31, 1989. In answering some of the questions you pose, I have avoided reiterating, to the extent possible, information already provided in the testimony and supporting material.

Q.1. How specifically is an institution to ascertain the credit needs of low- and moderate- income neighborhoods? How specifically will an examiner determine whether an institution has fulfilled this obligation?

A.1. The path to a successful and ongoing CRA program begins with an institution's efforts at ascertaining community credit needs, including those of the low- and moderate- income neighborhoods in the community it serves. These efforts will be somewhat different depending upon the size of an institution, its financial condition, and its location, among other variables. However, the key element in the ascertainment process is "outreach." A successful CRA effort requires that the institution's officers get to know the community and make meaningful contacts with local government officials and with community members, including groups, coalitions, and organizations that represent the interests of the community, including low- and moderate- income neighborhoods. The information derived from these contacts, in addition to analysis of demographic data, should form the basis for an effective assessment of community credit needs.

As part of the examination process, examiners explore the institution's activities to ascertain credit needs. Examiners accomplish this by reviewing the institution's own records and documentation, and by making contacts of their own to gain a perception of credit needs and how the institution has communicated with members of the community. OTS policy now requires that examiners make these outside contacts as a routine part of the CRA examination.

Q.2. Would marketing only to high income areas and not to moderate-income areas be non-compliance with the Community Reinvestment Act (CRA)? What sort of marketing is required?

A.2. Assuming that an institution had other than high income areas in its community delineation and its delineation was properly drawn, marketing efforts aimed only at high income areas would raise substantive concerns about an institution's commitment to meet community credit needs. The Act requires the agencies that enforce the law to assess an institution's record of meeting the credit needs of its entire community, including low- and moderate- income neighborhoods. However, neither the Act nor this agency's regulations require that a certain marketing plan or approach be utilized. The CRA examination procedures (submitted as part of my testimony) provide guidance to examiners in assessing whether an institution's marketing efforts are adequately designed to encourage applications for loans in its community, particularly low- and moderate- income neighborhoods.

Q.3. How do you analyze the geographic distribution of credit? How exactly is the HMDA data used? What would be an acceptable geographic distribution? What would be unsatisfactory? Provide several examples.

A.3. In addition to analyzing institution efforts at geocoding credit extensions, examiners typically utilize data compiled under the Home Mortgage Disclosure Act as well as data on non-HMDA loans to analyze the geographic distribution of credit extensions. The examiner cannot rely solely on HMDA information and must look at rejected loans as well as approved loans in order to come to any hypothesis about lending patterns for further testing.

In addition to HMDA data, OTS examiners have had access to application data compiled under our Loan Application Register/Data Submission Report System (see 12 CFR 528). This data provides examiners with information relative to where, and in what proportion, thrift institutions are serving all segments of their delineated communities. The data enables examiners to identify potential lending disparities on the basis of race, sex, marital status, and type of census tract. This aids substantially in the examiner's formulation of hypotheses for further testing. With the passage of FIRREA on August 9, 1989, financial institutions covered under the HMDA will be required to compile this type of information, in addition to data on the income levels of applicants beginning January 1, 1990.

Each institution's community delineation is different as is each community's demography. Consequently, it is very difficult to exemplify an "acceptable" or "unsatisfactory" distribution with any degree of exactitude. Essentially, a relatively even and balanced saturation of loans throughout all income and race categories would represent an ideal lending pattern, but it would not serve to indicate anything other than that - an institution could still be discriminating on a prohibited basis. On the other hand, if an institution seems to be granting a disproportionately low amount of credit in an area where credit demands are remaining unfulfilled, the institution should be encouraged to do more in meeting those credit needs.

Q.4. How many institutions have been approved without conditions when the financial institution has had a less than satisfactory rating?

A.4. Records on the number of approvals that have been granted to institutions with less than satisfactory CRA ratings have not been retained. Approvals for these actions were delegated to the Federal Home Loan Banks, and now to our District offices and no specific recordkeeping with respect to approvals vis a vis CRA ratings has been maintained.

Q.5. The March Joint Statement by the Exam Council encourages a dialogue between banks/thrifts and community groups through the expanded CRA statement and public comments thereon. Do you yet know how many banks and thrifts are now writing expanded CRA statements and how many are getting comments from community groups?

A.5. At this point, we do not have any information responsive to your question. We, too, are interested in the answer to this question and will explore ways in which we can capture that data.

Q.6. Describe how and when examiners contact community groups during an exam. How do examiners decide whom to contact? In what percent of exams are community groups interviewed? What are they asked?

A.6. Community contacts are made as part of the examiner's assessment of an institution's activities in determining credit needs and in helping to meet the credit needs of its community. Decisions as to whom to contact are within the purview of the examiner. However, our examination procedures indicate that the examiner is to interview a "sampling of community leaders and interest groups." Our procedures also provide examiners with a listing of the types of groups that they should interview.

Community contacts have been required as part of the CRA examination since April 1, 1989. The interview usually consists of asking questions to learn more about the local community, its sociology and its economy, and what the predominant community feelings about how well financial institutions are meeting credit needs. Given the relative newness of our specialized examination program, we do not have a tracking mechanism in place as of yet that would provide any statistics on these contacts. We intend, as part of our examination data system, to collect information on outside contacts and monitor our Districts' activity in this area.

Q.7. When the Federal Reserve Board reviews an application on CRA grounds, its order on the application routinely includes a discussion of the issues raised, the Board's assessment of the bank's performance with respect to those issues, and how its conclusions affected the final decision. This type of discussion has proved helpful - to lenders and community groups alike - in providing insight into the Board's interpretation of CRA. Are the other regulatory agencies willing to follow this practice?

A.7. If an application involves a CRA protest, or if the agency has any CRA concerns that would be evidenced by a denial of the application, the imposition of conditions on the applicant, or the offering of commitments by the applicant, OTS would include in the order its assessment of the CRA issues raised and how its conclusions affected its final decision.

Q.8. Since there are no performance standards for measuring CRA performance and assigning ratings, what assurance is there that ratings are assigned consistently by different examiners, within different regions of each agency, and across agencies?

In an area as subjective as CRA, there can be no absolute assurance that there will be consistency in the assignment of CRA ratings. Steps can be taken, however, to minimize inconsistencies and we have endeavored to do so in the following ways. First, we have a module in our basic compliance school that focuses on the CRA rating system through classroom discussion and an extensive case study. Second, we provide uniform guidance to all examiners on the CRA rating system through our Compliance Activities Handbook. Third, our internal review procedures include monitoring the District offices' adherence to our national standards in the compliance and CRA areas. These steps attempt to assure consistency throughout the entire agency.

On the interagency level, OTS, along with the FRB, FDIC, and OCC is in the process of developing a uniform CRA rating system in conformance with the requirements of FIRREA. This new rating system is being carefully crafted to provide as much guidance as possible to the examiners who will assign the ratings and to the public who will soon have access to them. One of the objectives of this exercise is to minimize the "gray" areas between rating categories such that clearer and more precise demarcations can be drawn, thus facilitating the assignment of the rating.

Q.9. Do financial institutions derive any benefits for achieving a top CRA rating? Should they? What specific recommendations would you have?

A.9. The institutions that we regulate do, in a sense, derive some indirect benefit from achieving top CRA ratings. First, institutions with outstanding CRA and compliance ratings are subjected to examinations on a less frequent basis than those with lower ratings. Second, absent a CRA protest or other problems of a financial nature, an application involving an institution with a satisfactory CRA performance record is likely to be processed with fewer hitches.

It is my personal belief that institutions should not receive any direct benefit for upholding compliance with a law and fulfilling its mandate. It is each institution's basic obligation to do all it can to improve the community it was chartered to serve, consistent with safe and sound operation.

Q.10. Some banks claim that their CRA ratings have been downgraded because of agency criticism of their documentation. This apparently has occurred even when the bank in question was performing on CRA in a superlative manner. How much new emphasis is being placed on CRA documentation as opposed to performance? How do you balance the two?

A.10. We are not aware of any situations involving thrift institutions where CRA performance was downgraded due to an inability to adequately document CRA activities. The examiner needs to consider an institution's documentation of its CRA-related activities along with information gleaned from other sources in order to arrive at a balanced overall assessment. Institutions can certainly assist in the process by being encouraged to provide as much information on CRA activities as possible in an organized, coherent fashion. This documentation provides the examiner with a better basis to make judgments about the effectiveness of an institution's overall CRA program. An institution's overall CRA performance, however, is certainly more important to us than its ability to adequately document its CRA activities.

Q.11. Do agency procedures require examiners to review existing CRA agreements between lending institutions and community groups? If so, describe the procedures. Do examiners routinely assess a financial institution's implementation of such an agreement in evaluating an institution's CRA performance? Do the procedures require examiners to contact the community groups as part of this evaluation?

A.11. Our CRA examination procedures do not explicitly require examiners to review private agreements between lenders and community groups. During the course of a CRA examination, however, examiners should take the existence of such an agreement into consideration when formulating a performance assessment. A discussion with an applicable community group may aid in reaching CRA conclusions. We will consider revising our procedures to make mention of private agreements as well as the role that such agreements should play in the assessment process. We do not believe that examiners or regulatory agencies should be placed, however, in the position of enforcing private agreements and any procedures we might develop would be tempered by that position.

Q.12. All of the agencies indicate that HMDA data is integral to CRA evaluations and helps them to determine the degree to which lenders are serving various parts of their communities with respect to mortgage loans. Would comparable data for commercial lending be equally useful? If not, why not?

A.12. Historically, thrift institutions have been primarily engaged in housing-related finance and will continue to focus on that type of lending. HMDA-type data on commercial loans would not be very useful for us since only about two percent of our total institution assets are in commercial loans (based on 1987 data).

Q.13. A recently released study by the Center for Community Change found that banks and thrifts lend, on average, 3 times as much in white middle class neighborhoods than in minority middle class neighborhoods. Why does this sort of redlining still exist? Should not enforcement of CRA laws stop redlining?

A.13. The Center for Community Change's study, as well as news media reports such as those that appeared in the Atlanta Journal and Constitution point out that there may, in fact, be disparities in the availability of mortgage related credit on basis of race, property location, or both. We are deeply concerned about these types of reports and we are committed to the vigorous enforcement of the fair lending laws by investigating the allegations about the lending patterns of thrift institutions.

Q.14. Each agency's testimony provided data on how many hours examiners spend per CRA exam. Clarify your methodology, as it is uncertain whether each agency followed the same methodology in calculating the hours.

A.14. Exhibit F of my testimony provides the average number of hours spent in each institution examined during a given year on CRA according to certain asset size ranges. To illustrate our methodology, we informed you that in 1983, our District offices spent 3.66 hours on average performing examination procedures for CRA in institutions with assets of less than $25 million. This figure was derived by dividing the total CRA examination hours spent in institutions with less than $25 million in assets in 1983 by the number of institutions examined during 1983 with less than $25 million in assets.

Q.15. In the past four years the Bank Board has had 3515 applications, of which 3 were denied on CRA grounds and 7 were approved with conditions. The remaining 3505 were approved without conditions. Compare these statistics with applications subject to a protest: more than half (5 of 9 protested applications) were approved with conditions. Is it Bank Board policy generally not to attach conditions unless an application is protested?

A.15. There is no Bank Board policy that would generally preclude the use of conditions in nonprotested applications. As indicated in my testimony, satisfactory CRA performance is a required regulatory criterion in many types of applications involving federally-insured institutions. If the CRA rating of an institution is satisfactory, CRA does not become a regulatory issue as part of the applications process, unless, of course, the application is protested or more recent adverse information is presented. As you are aware, in the majority of cases, institutions have been assigned satisfactory CRA ratings. Consequently, one would not expect to find CRA-related conditions attached to the majority of approved applications.

Q.16. The Bank Board regularly grants requests for extending comment periods and for holding hearings. Have there been problems with this policy? Have the hearings resulted in delays in processing applications or not? Have the hearings helped the Bank Board in evaluating applications?

A.16. We are not aware of any instances where the agency's decision to extend a comment period or hold an oral argument has presented a problem for commenters or protestants. In some instances, applicants have complained that the extension or the decision to hold an oral argument will delay the eventual decision on an application. This is a natural consequence but the agency believes that affording the public additional time to comment on an application or providing for an oral argument has proven to be worthwhile.

An oral argument provides an arena for protestants who frequently believe they have been unable to obtain an adequate hearing from the institution or its regulator. The oral argument should take place from 10 to 60 days after the decision to hold one is made. If serious negotiations have been initiated between the applicant and protestant, the oral argument is sometimes delayed to allow the negotiations to proceed, so that the parties can find their own best resolution. The need to analyze and resolve substantive issues, whether through negotiation or administrative action, usually requires more time than the oral argument process itself.

The oral argument provides an opportunity for face-to-face discussion among all parties: applicant, protestant, and regulator. Especially if the protestants are not represented by legal counsel, or the equivalent, it also provides them with an important opportunity for oral elaboration of their written documents.

Q.17. Provide examples of supervisory actions the Bank Board has taken outside the application process. Under what conditions will you take supervisory action, and in what percentage of cases have you done so?

A.17. The CRA makes it clear that its enforcement leverage is linked to the applications process. There have been no instances where the Bank Board used its formal enforcement authority to address CRA matters (presumably the focus of your question). The agency could use its authority to address correction of technical violations of our CRA regulations (i.e., the notice and statement provisions).

Q.18. Page 17 of your testimony states that the Bank Board may invoke its cease and desist authority if an institution does not fulfill the terms of a condition. Has this authority ever been exercised?

A.18. Again, we are presuming that your question relates to CRA-related conditions. We have not found it necessary to invoke our cease and desist authority for an institution's failure to fulfill the terms of a CRA-related condition.

Q.19. What efforts are made to assure uniformity of ratings and examination criteria among different regions. Exhibit D to your testimony shows, for example, that no institution received an unsatisfactory rating in district 3 while district 11 consistently had the highest number of unsatisfactory ratings (in 4 of 5 years with at least 10% unsatisfactory ratings in the past 3 years). Do district 3 thrifts comply better with CRA than those in district 11 or are examiners using different standards of enforcement?

A.19. We cannot say whether thrift institutions in District 3 have better performance records than those in District 11. We can, however, repeat the primary message of our testimony - this agency diverted much of its available resources over the past decade to the burgeoning thrift crisis and was not able to devote as much attention to the CRA and compliance areas as it would have liked. Consequently, while each District had the same CRA procedures to work with, the amount of emphasis that each District was able to place on CRA varied, thus resulting in uneven work products from one District to another.

As mentioned earlier, several factors should serve to minimize these types of disparities in the future. We now have a uniform, national examination program in place for the compliance and CRA areas with the concomitant training and oversight necessary to make this a successful and responsible undertaking. As a result of FIRREA, we are participating in an interagency exercise to develop a uniform CRA rating system.

Q.20. Explain how Leader Federal Bank for Savings was able to open a branch office the day after the Bank Board rejected its application to open another branch on the grounds the conditions established for the initial branch opening had not been met. What measures will the new Office of Thrift Supervision be taking to monitor conditional approvals?

A.20. Essentially, the supervisory agent at the Federal Home Loan Bank of Cincinnati responsible for Leader made the determination that the institution had substantially met the CRA conditions imposed by the Bank Board in May 1988. This decision enabled Leader to open the branch. The authority to make such a determination had been delegated by the Bank Board to the supervisory agent.

In its ruling of July 19, 1989, the Board determined that while Leader had made progress toward meeting the previously imposed conditions, the progress had not been sufficient to justify additional approvals by the Board. Several major items, which appeared to be in progress at the time of the supervisory agent's previous branch approval, were still not completed at the time of the Board's decision. In addition, a recent examination, completed in the interim, raised some new issues. As a result, the Board rejected the application under review and advised Leader not to open the other branches covered by the 1988 resolutions until the Board or its successor determines that all pertinent concerns have been addressed.

We believe it is appropriate for the supervisory personnel of the District offices to continue to monitor conditional approvals, including conditions related to CRA. However, we also believe that a better degree of coordination between the Washington and District offices for monitoring particularly sensitive issues, such as those that sometimes arise in connection with CRA matters, would serve to strengthen this system.

I trust that these answers are responsive to your inquiry. If I can provide any additional information, please let me know.

Sincerely,

Jerauld C. Kluckman
Acting Director
Division of Compliance Programs

QUESTIONS FOR JOHN H. McDOWELL FROM SENATOR ALAN J. DIXON
JULY 31, 1989

1. **How specifically is an institution to ascertain the credit needs of low- and moderate-income neighborhoods? How specifically will an examiner determine whether an institution has fulfilled this obligation?**

National banks are responsible for ascertaining the credit needs of their local communities, including low- and moderate-income neighborhoods. They are also responsible for determining how to ascertain those needs. While some banks may use sophisticated market research to identify credit needs, we encourage all banks to meet with local entities such as merchants' associations, state and local government officials, community development organizations, civil rights groups, neighborhood and housing development organizations, and minority and small business associations. Local organizations such as these are best able to provide a bank with information on the credit needs of the local community.

Examiners review bank records, interview bank personnel, and, in some cases, meet with local organizations such as those identified above to determine the extent to which a national bank has attempted to identify local credit needs. And, most importantly, examiners will determine how senior management and the board of directors have responded to any identified local, unmet credit needs.

2. **Would marketing only to high income areas and not to moderate-income areas be non-compliance with the Community Reinvestment Act (CRA)? What sort of marketing is required?**

Marketing only to high income areas would be in non-compliance with the intent of the CRA. All national banks subject to the Community Reinvestment Act have an affirmative obligation to help meet the credit needs of their entire community, consistent with safe and sound operations. While no specific marketing is required, all banks are encouraged to make an effort to ensure that the entire community, including residents of lower income neighborhoods are aware of products and services they offer.

Examiners review marketing policies and strategies to determine if they are designed to inform the entire community of the credit services offered. Some of the marketing activities include:

- Any working relationships the banks may have with real estate brokers or others who service low- and moderate-income neighborhoods;

- Mortgage counseling programs and programs of management assistance for small or minority businesses;

- Credit and credit-related services in low- and moderate-income neighborhoods compared to such services in other neighborhoods served by the bank;

- Advertising the types of loans the bank is willing to make in media likely to reach low- and moderate-income individuals in the bank's local community; and

- Availability of convenient hours in offices accessible to residents of low- and moderate-income neighborhoods.

3. **How specifically do you analyze the geographic distribution of credit? How exactly is the HMDA data used? What would be an acceptable geographic distribution? What would be unsatisfactory? Provide several examples.**

For national banks subject to HMDA, examiners can review the analysis of mortgage lending prepared by the bank, if available. If the bank has not analyzed its HMDA data, the examiner will evaluate the geographic distribution of real estate loans using the bank's HMDA statement, the HMDA Aggregation Tables and demographic data about the bank's local community from the most recent census to determine where the bank made its loans. For banks not subject to HMDA or for credits other than real estate loans, examiners rely on other information such as indications of out of area lending by analyzing, for example, summary reports of consumer or small business loans.

Examiners will also review a bank's credit policies to ensure that they do not have the effect of denying access to credit to residents of lower income neighborhoods. Additionally, to identify any adverse effects on lower income neighborhoods, examiners review the bank's record of opening and closing branch offices and of providing services.

In assessing whether a national bank's geographic distribution of loans is acceptable or unacceptable, an examiner must first determine whether the institution's community delineation is appropriate. In other words, is the institution capable of adequately serving the entire community or is the delineation too large or too small for the institution's financial capabilities. Examiners must also review the demographics of the bank's location to determine if there are any low- to moderate-income areas and, if so, whether they have been arbitrarily excluded from the community delineation. A bank's marketing efforts must also be evaluated. Examiners assess whether the bank has adequately developed and marketed its products and services in response to identified credit needs in all segments of its community.

The number, type and geographic distribution of loans may differ for each institution based on its resources, capabilities, the products and services it offers and its local community's credit needs. Examiners are trained to incorporate these differences into their overall assessment of the bank's performance.

Assume for this discussion, that a financially sound national bank with $250 million in assets has delineated its community as the county in which it is located. The county includes low- to moderate-income census tracts. The national bank examiners have determined that the bank's community is appropriately delineated. Examiners then review the bank's analysis of its lending activity to determine if all segments of the community, including low- to moderate-income areas, are receiving lending activity. The review includes an analysis of applications received and the credit standards applied to the applications to ensure that they are not illegally discriminatory. If the analysis reflects that lending activity is occurring in most segments of the community including the low- to moderate-income areas, it is deemed acceptable.

Conversely, assume that bank management has documented its efforts to ascertain the credit needs of its delineated community, but its marketing efforts are directed only to a very specialized segment. The types of credit the bank is willing to offer and extend appear to be inconsistent with those desired and needed within its community. Thus, only a small percent of the bank's total loans are to customers within the delineation. A lack of loans or low loan demand in low- and moderate-income areas, in the absence of efforts to market loans in those areas, would be deemed unacceptable. Based on the bank's marketing efforts, and the current composition and geographic distribution of its loans, management has not demonstrated that it is sufficiently committed to comply with the spirit or intent of CRA.

4. **How many applications have been approved without conditions when the financial institution has had a less than satisfactory rating?**

Based on an investigation of files and other records from January 1, 1987 through August 31, 1989, the OCC approved without conditions 66 applications from 30 national banks with less than satisfactory CRA ratings. No approvals were given to banks with 5 ratings. One approval was granted to a bank with a 4 rating. The approval was for a branch that was being established as part of the bank's plan to improve its CRA performance. The remaining approvals were granted to banks with 3 ratings. In one case, the approval involved the acquisition of a failed bank. For most others, the Office determined that sufficient evidence of improvement in performance was available to permit the OCC to grant an approval without conditions although the banks had 3 CRA ratings at the time of approval.

5. **The March Joint Statement by the Exam Council encourages a dialogue between banks/thrifts and community groups through the expanded CRA statement and public comments thereon. Do you yet know how many banks and thrifts are now writing expanded CRA statements and how many are getting comments from community groups?**

   It is too early to tell how many banks are expanding their CRA statements to incorporate the information suggested in the CRA Joint Policy Statement. However, we have received requests from banks to provide further guidance on expanding their CRA statements.

6. **Describe how and when examiners contact community groups during an exam. How do examiners decide whom to contact? In what percent of exams are community groups interviewed? What are they asked?**

   Meetings with community groups are performed during an examination when the examiner determines that there is insufficient information to objectively assess the bank's CRA performance or determine whether a bank has engaged in illegal discriminatory practices. Additionally, examiners may conduct outside inquiries to determine the validity of a concern regarding the bank's CRA performance raised by a person or organization. For instance, concerns about a lack of mortgage financing might require discussions with non-profit housing development corporations, a Neighborhood Housing Services group, local realtors or the local government housing agency.

   Each of OCC's six district offices also maintains an ongoing program of outreach efforts. This is an efficient way to obtain information about entire communities served by several national banks and provides an information base for adequate CRA and fair lending analysis. Discussions are normally held with community development organizations, consumer, neighborhood and small business groups and housing related organizations. Questions from the examiners center on the groups' perception of unmet credit needs that may exist in their community and how well they believe banks are meeting community credit needs; the types of marketing efforts the local national banks undertake to address the credit needs of the community including the low- and moderate-income areas; and, if small business lending concerns are being addressed, the types of standards or requirements that exist for this type of lending.

   This office does not track the number of CRA examinations where outside contacts were made.

7. **When the Federal Reserve Board reviews an application on CRA grounds, its order on the application routinely includes a discussion of the issues raised, the Board's assessment of the bank's performance with respect to those issues, and how its conclusions affected the final decision. This type of discussion has proved helpful -- to lenders and community groups alike -- in providing insight into the Board's interpretation of CRA. Are the other regulatory agencies willing to follow this practice?**

The OCC recently revised its procedures for disclosure of corporate application decisions involving CRA considerations to provide easier access to the information for national banks and the public. As described in Banking Circular 238 (**Appendix 1**), the Office will publish decision letters for all cases in which corporate applications from national banks have been conditionally approved or denied on grounds related to CRA. Such letters will be published monthly in an existing OCC publication titled Interpretations. In addition, all such decisions will be summarized in the OCC's Quarterly Journal, in a separate subdivision of the section on "Recent Corporate Decisions". The Office believes that publication of these letters transmitting its conditional approval and denial decisions, the findings behind those decisions, and conditions to the decision (if applicable), will convey information and guidance on the OCC's CRA-related decisions and its use of assessments of CRA performance in deciding covered corporate applications.

8. **Since there are no performance standards for measuring CRA performance and assigning ratings, what assurance is there that ratings are assigned consistently by different examiners, within different regions of each agency, and across agencies?**

Although there are no quantifiable standards for CRA performance, in 1981 the financial regulatory agencies adopted the Uniform Interagency CRA rating system (**Appendix 2**). The system requires rating five performance categories, or components, under which the 12 assessment factors of CRA are grouped. A thorough description of the characteristics for each of the ratings is included in the system and financial institutions must exhibit those characteristics to receive that rating. We believe that no system would guarantee complete consistency between examiners, districts, or agencies, but this rating system does provide sufficient guidance to alleviate significant deviations and at the same time provides examiners with the necessary flexibility to adapt to different bank structures and their corresponding communities' needs.

9. **Do financial institutions derive any benefits for achieving a top CRA rating? Should they? What specific recommendations would you have?**

Currently, the only benefit a bank receives from a satisfactory or better performance rating is that, absent a CRA protest or other public comment opposing the bank's application, decisions on corporate applications are not delayed because of CRA considerations. We do not believe that further rewards or benefits are warranted.

10. **Some banks claim that their CRA ratings have been downgraded because of agency criticism of their documentation. This apparently occurred even when the bank in question was performing on CRA in a superlative manner. How much new emphasis is being placed on CRA documentation as opposed to performance? How do you balance the two?**

We have always encouraged national banks to document their performance to demonstrate how well they are helping to meet the credit needs of their community. Without this documentation, it is very difficult for examiners to assess the bank's level of CRA performance. Because it is bank management's responsibility to comply with the law, it is also the bank's responsibility to document its performance. Documentation of a bank's efforts provides management with key information necessary for setting policies, strategies and for self-monitoring. Therefore, we believe it is appropriate for the CRA rating to reflect the bank's efforts to document the level of CRA performance. Additionally, if a bank documents its CRA-related activities it will be in a far better position to respond to the issues and concerns raised by consumer and community groups, especially in a protest situation. For these reasons, we believe it is critical for banks to document their CRA efforts.

11. **Do agency procedures require examiners to review existing CRA agreements between lending institutions and community groups? If so describe the procedures. Do examiners routinely assess a financial institution's implementation of such an agreement in evaluating an institution's CRA performance? Do the procedures require examiners to contact the community groups as part of this evaluation?**

The OCC's examination procedures do not require that examiners review existing CRA agreements between lending institutions and community groups. Such agreements are not subject to OCC approval or enforcement. When assessing the bank's record of meeting its local community credit needs, the OCC will consider evidence presented to us, by the parties to the agreement, as to whether the bank has adhered to the agreement.

12. **All of the agencies indicate that HMDA data is integral to CRA evaluations and helps them to determine the degree to which lenders are serving various parts of their communities with respect to mortgage loans. Would comparable data for commercial lending be equally useful? If not, why not?**

We agree that an analysis of HMDA data to determine the penetration levels of mortgage lending in a bank's market area is a good indicator of whether a bank is serving its entire community including low- and moderate-income neighborhoods. Our examination procedures require that examiners review a bank's credit applications, extensions and denials and determine if that distribution would indicate a failure to serve selected areas of the bank's local community. Depending on how the bank has defined its business niche, this may include HMDA data, small business lending, credit card activity or personal, unsecured credit. Analysis of the various commercial types of credit offered by the bank would be beneficial in reaching conclusions about a bank's lending activity, but we believe the cost of collecting and maintaining the information would exceed its CRA-related benefit.

13. **A recently released study by the Center for Community Change found that banks and thrifts lend, on average, 3 times as much in white middle class neighborhoods than in minority middle class neighborhoods. Why does this sort of redlining still exist? Should not enforcement of CRA laws stop redlining?**

We do not believe available data is sufficient to conclude that redlining exists although it does indicate that depository institutions may not be effectively marketing their products in minority neighborhoods. In particular, the various studies do not consider lien transfer information. They also do not consider the competition from nondepository institution mortgage companies who specialize in VA and FHA loans that may be more attractive to some borrowers. Attached is a copy of OCC's analysis of an earlier study reported in the "Atlanta Constitution" that examines some of these issues **(Appendix 3)**.

14. **Each agency's testimony provided data on how many hours examiners spend per CRA exam. Clarify your methodology, as it is uncertain whether each agency followed the same methodology in calculating the hours.**

As we mentioned in our testimony, the OCC does not have precise information on the amount of time devoted specifically to CRA examinations. The calculations we provided were based on our estimate that approximately 20 percent of the time spent on the consumer protection portion of a compliance examination is devoted to CRA. The following table provides information on the average examination hours spent on CRA related examinations during 1987 and 1988. We translated examiner work days provided in the testimony into examiner hours by multiplying previously provided data by eight.

Examiner Hours Devoted to CRA Examinations
by National Banks' Asset Size

Asset Size	Examiner Hours Per Bank Examined 1987	1988
Under $50 million	20	16.0
$ 50 million to $100 million	20	21.6
$100 million to $300 million	24	27.2
$300 million to $1 billion	36	44.8
$1 billion to $10 billion	72	64.8
Over $10 billion	132	168.0

15. **The OCC's testimony seems to state a policy about denials of applications which differs from the other regulators. Your testimony states that denying an application is a last resort and that conditional approvals are more effective in promoting CRA compliance. The testimony of the Federal Reserve and the Bank Board indicates that those agencies give some weight to commitments offered by an applicant to rectify deficiencies only if the CRA performance is otherwise generally satisfactory. That testimony would imply that an application is judged on an institution's record and not on future commitments, unless only a few, smaller matters need improvement. Should not banks and thrifts with good records be treated better than institutions which promise to comply with CRA only when they have an application pending? Clarify your policy in relation to the other regulatory agencies.**

The OCC was a signatory to the March 1989 Statement of the Federal Financial Supervisory Agencies Regarding the Community Reinvestment Act (Appendix 4). That Statement articulates a position on the role of commitments for future action which accurately reflects the position of the OCC. Commitments for future action cannot be used to overcome a seriously deficient record of performance, and in such situations denial would be an appropriate response. However, as discussed in the joint statement, the Office may require financial institutions to take specific actions designed to improve CRA performance by granting approval of an application, conditioned upon the bank taking certain steps to improve its CRA performance prior to consummation of the transaction. Further, the OCC has denied bank applications when the situation warranted it. Five applications have been denied on CRA grounds as of December 31, 1988; two were denied in 1981; one in 1986; and, two in 1988.

16. Your testimony states that the OCC has provided speakers for over 60 seminars and training sessions in the past two years. Approximately what percentage of banks which the OCC supervises attended such seminars?

Most of the seminars and meetings for which the OCC provided speakers were sponsored by state bankers and trade associations that have members from virtually all sectors of the financial services industry. To estimate what percentage of the participants represented national banks is not possible.

17. Pages 3-4 of your testimony state that over the first approximately 20 months of the compliance program, the OCC took 17 enforcement actions "solely on the basis of identified compliance problems" and another 208 enforcement actions "partially" on such basis. What does that mean? In those 20 months how many banks were examined? Provide examples of some of these supervisory actions.

The results of an examination may indicate a bank has significant compliance problems requiring an enforcement action based solely on that particular problem. For instance, an enforcement action was taken on a bank which required correction of significant violations of the Equal Credit Opportunity Act and the establishment of systems and policies to prevent recurrence of these violations. In most cases, however, compliance related provisions are included in enforcement documents that are initiated for both safety and soundness and compliance concerns. For example, these actions may include provisions that require the bank to establish a committee to oversee the compliance function. The Compliance Committee is then required to report to the Board of Directors on a specified periodic basis concerning its efforts to develop a comprehensive compliance program with adequate policies and procedures. The Board of Directors would then be required to formally adopt such a plan and include the approval in their minutes. The bank would also be required to report on its activities to the OCC's supervising office on a periodic basis. From the Compliance Program's inception in April, 1987 through year-end 1988, 1140 compliance examinations have been conducted.

18. How does the OCC monitor conditional approvals and commitments? What specifically has the OCC done if an institution does not comply with commitments it makes?

When conditional approval is granted, a method for demonstrating or reporting compliance with the condition(s) is detailed in the decision transmittal letter. Final approval is not granted, or consummation of the approved transaction is not permitted, until the bank has provided the required documentation of compliance. The OCC will send examining staff on-site, if necessary, to verify compliance with the conditions.

19. What percentage of banks that the OCC supervises participate in one form or another in a community development corporation (CDC)? Do you believe it appropriate if a bank's only CRA lending is through a CDC? If so, how does the OCC judge what would be an appropriate level of participation for a bank of a specified size?

The OCC approves national bank equity investments and some debt investments in community development corporations through the National Bank Community Development Corporation and Investment Program. Interpretive Ruling 7.7480 and Banking Circular 185, which guide the program, enable banks to carry under "Other Assets" investments in programs and projects which primarily have a public or community purpose. Banks have used the program to create wholly-owned CDC subsidiaries, to invest in multi-bank CDCs, to invest in existing community-based CDCs and to invest in limited partnerships. These organizations have undertaken activities including: comprehensive economic or housing development strategies in declining areas; rehabilitation and construction of low- and moderate-income housing; and special programs for emerging small businesses. As we indicated in our testimony, 130 national banks have invested equity or debt (as of July 1, 1989) in CDCs through this particular program. This is virtually three percent of all national banks.

However, many national banks participate in community development corporations without using the OCC's CDC Program. If they make charitable contributions, there is no requirement for OCC approval. In addition, banks may make loans to CDCs, consistent with regular bank lending policies, without OCC approval. We do not track the number of bank loans or the number of contributions to community development corporations.

National banks receive OCC approval for debt or equity investments in CDCs to carry out public purpose activities which either cannot be carried out within the bank or which are innovative responses to community needs. These CDC investments are made to complement regular bank community lending activities, not replace them.

When the OCC reviews a bank's CRA performance, we evaluate the bank's unique capacities, the special needs and investment opportunities in its community, and how the bank identifies and helps address those needs and opportunities, including the bank's participation in various forms of local community development programs.

The OCC does not believe that a national bank's only "CRA lending" should be administered through a CDC subsidiary or through a CDC in which it invests with others. CRA indicates that regulatory agencies are responsible for encouraging the banks they regulate to help meet the credit needs of their local communities, including those of low- and moderate-income areas. National banks should evaluate all of their lending areas and approaches and take steps to assure that all the credit products they offer are accessible to qualifying applicants in all parts of their local communities. They have an obligation to assure that they understand the credit needs of the entire community and to develop ways to respond, consistent with the expertise and resources of the institution.

Separating all "CRA lending" into a CDC does not promote this kind of comprehensive view of CRA responsibilities and could tend to limit unnecessarily a bank's CRA efforts to those defined as "community development".

Interpretive Ruling 7.7480 clearly indicates that investments in CDCs or community development projects are permitted "wherein the bank will receive an equity interest in or evidence of debt which may have value in the future but which is clearly not a bankable asset by ordinary standards." OCC Banking Circular 185 makes it clear that "national bank investments in CDCs or CDC-sponsored projects are intended to stimulate, not compete with, private sector investment or development companies." When a national bank organizes a CDC, it is asked to explain how the CDC will supplement, and not replace, lending or investment activity that can be undertaken by the private market, and the bank itself. National bank investments in all CDC subsidiaries and projects under Interpretive Ruling 7.7480 are limited to five percent of capital because these investments are expected to go beyond ordinary banking activities. However, there is no reason to place that kind of limit on "CRA lending" generally.

On the other hand, a bank's CDC subsidiary or its participation in a CDC with other investors can have a significant impact on its CRA assessment overall. By developing special programs targeted to meet the needs of customers that would not otherwise have access to the bank (i.e. very new businesses or small nonprofit organizations) the bank CDC may serve as a bridge to facilitate direct financing by the bank itself.

For example:

- o New small businesses may receive longer term or subordinated loans from a CDC and thereby qualify for regular lines of credit from the bank itself; or
- o A small nonprofit, with limited development experience and financial resources, may receive construction loans and technical assistance from a CDC and the bank's real estate loan department may make mortgages to low- and moderate-income purchasers of the housing constructed by the organization.

20. **Unlike the other regulatory agencies, OCC uses a random sampling technique for selecting national banks (with under $1 billion in assets) for compliance examinations. What percentage of banks are examined in any given year? For how many years might a bank not be examined? Does the OCC intend to change this policy as a result of the recent legislation requiring public disclosure of CRA ratings and evaluations?**

One half of all national banks and national bank holding companies with total assets of $1 billion or more are examined each year, with lead banks and individual subsidiaries and affiliates examined on a

case-by-case basis. Sixteen percent of all other banks are examined each year. We estimate that institutions representing over 40 percent of national bank system assets, or over $730 billion, are covered by examinations conducted under the Compliance Program each year.

Because community banks (banks with less than $1 billion in assets) are selected randomly, it is conceivable that a bank would not appear in the sample for two, three, or even more years. If a bank is not included in the Compliance Program sample, it is still subject to supervision for compliance. For example, during the second 12 months of the Compliance Program, compliance with consumer protection legislation was monitored in over 1200 national banks and compliance with commercial activity regulations (e.g., those implementing the Bank Secrecy Act) was monitored in over 1700 national banks. During the first year of the Compliance Program, approximately 30 percent of over 225 staff years devoted to supervising applicable compliance subject areas was expended in banks not examined under the program. By the second year of the program, this figure was up to almost 37 percent -- including follow-up efforts to ensure that problems found the first year had been corrected.

In short, our supervisory approach for promoting and monitoring compliance is not limited to a sample of national banks; our examinations and other supervisory activities are designed to have all banks comply with the law.

Questions for the record for the FDIC from Senator Dixon
from July 31, 1989 hearing

Q.1. How specifically is an institution to ascertain the credit needs of low- and moderate-income neighborhoods? How specifically will an examiner determine whether an institution has fulfilled this obligation?

Financial institutions are expected to be familiar with the revised interagency CRA Statement (issued on March 21, 1989), particularly the section on "Developing an Effective CRA Process". While the FDIC does not require any one particular method or procedure to be used by an institution in determining the credit needs of low- and moderate-income neighborhoods, we do require that the methods used accommodate the varying circumstances and unique characteristics of individual institutions and neighborhoods. Essential to the ascertainment of local credit needs is ongoing institution outreach and communication with community members and representatives from local governments, businesses, and community-based organizations. Local individuals and groups should also be able to initiate communication with officers of local financial institutions regarding CRA. Communication may take the form of (but is not limited to) interviews, meetings and studies, such as surveys.

In addition, an institution may review relevant census data and the Home Mortgage Disclosure Act (HMDA) aggregation tables to ascertain present and future home loan demand. Institutions may also review property tax transfer data maintained by local jurisdictions. If, for example, properties are being sold but not financed through local institutions, this could be an indication that bankers may not be responding to local housing-related credit needs. Economic forecasts and housing studies developed by the planning departments of local governments may also be used.

The FDIC's CRA implementing regulation, 12 CFR Part 345, requires that specific CRA assessment factors be evaluated in the determination of an institution's record of CRA performance (Attachment A). The FDIC evaluates the institution's record of performance relative to each assessment factor through the use of the Interagency CRA Assessment Rating System. Five Performance Categories are currently being used in this rating process, with the first of these focusing directly on community credit needs and marketing. FDIC examiners use both the CRA examination procedures and CRA rating system to determine whether an institution has fulfilled its obligations to ascertain the credit needs of the low-and moderate-income community. A copy of both the CRA examination procedures and the CRA rating system is attached.

FDIC examiners review and evaluate activities conducted by the institution to determine whether the credit needs of an institution's community are being addressed. This includes the extent of the institution's efforts to communicate with members of its community, including low- and moderate-income members,

regarding the credit services being provided by the institution. FDIC examiners obtain this information from the institution's records and through interviews with a representative sample of persons with whom the lender has said it has communicated in ascertaining local credit needs. To ascertain credit needs, an institution's efforts may include, but are not limited to, communication with: customers; educational organizations; local government officials, including housing and planning staffs; merchants' associations; religious organizations; block clubs; neighborhood organizations; local civil rights, consumer, minority, and non-English speaking groups; housing counseling service centers; community development corporations; nonprofit housing development corporations; and local development corporations. Studies used by the institution concerning local credit needs are examined. Further sources of information concerning local credit needs may be found in any signed comments received in response to the institution's Community Reinvestment Act (CRA) statement and in consumer complaints concerning the institution.

Q.2. Would marketing only to high income areas and not to moderate income areas be noncompliance with CRA? What sort of marketing is required?

The type of marketing viewed positively by the FDIC is that which causes members of an institution's total delineated lending community to become aware of the credit services offered by that institution. Examples of appropriate marketing efforts may include making marketing presentations to low- and moderate-income community groups, real estate brokers, local businesses (including small businesses and small farms where such exist) and to neighborhood, religious, and minority organizations. In addition, providing educational brochures and other materials to community groups is encouraged. The FDIC CRA examination procedures indicate the type of actions the FDIC will consider favorably in evaluating an institution's performance. One crucial point addressed in the CRA examination procedures is that the advertising of the types of loans the institution is willing to make should reach low- and moderate- income individuals in the institution's local community. Under the CRA rating system, marketing performance is also evaluated.

An institution would be in noncompliance with the CRA if low- and moderate-income areas were included as part of an institution's community delineation and then ignored by that institution. Not marketing in the low- and moderate-income areas of a lending area, while marketing in high income areas, is considered by the FDIC as antithetical to the purposes of the CRA. It is clear that the community delineation developed in response to CRA requirements must not unreasonably exclude low- and moderate-income neighborhoods. Therefore, an institution would not be in compliance with the CRA if a low- or moderate-

income neighborhood were arbitrarily excluded from the definition of an institution's local community delineation and therefore, not included in marketing efforts.

Q.3. How specifically do you analyze the geographic distribution of credit? How exactly is the HMDA data used? What would be an acceptable geographic distribution? What would be unsatisfactory? Provide several examples.

To understand what an examiner uses to assess an institution's record of performance, see the attached FDIC CRA examination procedures (Attachment B) and CRA rating system relative to determining and evaluating an institution's geographic distribution of credit (Attachment C). The goal here is for the institution to make appropriate portions of credit available to all areas within its identified lending community. Evidence to determine appropriate (i.e., fiscally sound and reasonable) geographic distribution is to be found in the institution's credit extensions, applications and denials. The determination of what constitutes an acceptable geographic pattern of lending under the CRA is relative, based on an evaluation of the interplay of pertinent factors, such as the institution's housing lending efforts relative to loan demand, the financial position of the institution, and credit commitments as outlined in the institution's CRA statement.

From a regulatory standpoint, HMDA statements serve as a tool for closer analysis, if and when problems concerning an institution's CRA compliance are suspected. The HMDA statement is generally considered a reliable indication of the number and dollar amount of mortgage loans extended in an institution's lending area. HMDA aggregation table data is provided to field examiners. By using this data, examiners can get an estimate of housing loan activity for the more urban institutions by census tract.

Currently, FDIC examiners use HMDA data to compare the lending patterns of the bank being examined against those of competing institutions in the lending area. If it is seen that competing institutions are making loans in what have been identified as low- to moderate-income census tracts and the institution being examined is not, examiners will explore the reasons behind the discrepancy.

While such a discrepancy could be interpreted as suspicious, a lending institution could contend that: a) despite acceptable outreach efforts, the loan demand from these areas was not forthcoming; or b) the creditworthiness of applicants from these areas disallowed acceptance. Depending on the types of credit the bank offers, the degree of difference in apparent performance among similarly situated lenders, and the overall compliance performance of the bank being examined, the FDIC

examiner may undertake an in-depth examination which could entail a geocoding of loan applications received. If disparate lending patterns are found, an analysis would be made of the reasons for denial and the validity of such reasons, as compared to the characteristics among the applications approved.

By way of further example, a review of an institution's HMDA statement may reveal a disproportionately low number of loans in low- or moderate-income areas relative to other areas in the community. If such a trend is found, FDIC examiners investigate further into the reasons for any such pattern. If such a lending pattern cannot be justified, this would serve as a basis for a less than satisfactory CRA rating. The FDIC would then advise the institution to improve its record by seeking to meet the credit needs of all segments in its lending community by applying the specific elements of an effective CRA process as outlined in the revised interagency CRA statement.

Although HMDA statements alone are not capable of supporting conclusive interpretations (e.g. that solely on the basis of few loans in low- or moderate-income areas relative to other areas, there has been a violation of CRA or fair lending laws), a HMDA statement which leads to questions about an institution's lending patterns serves as a valuable indicator for FDIC examiners. It causes an examiner to research, for example, whether omitted census tracts are indeed zoned residential, whether an institution's advertising of loan programs is actually reaching residents of these locales, and whether any demand for loans has emanated from these areas and, if not, why not. These questions tie in directly with other CRA assessment factors. Negative findings based on these factors have resulted in FDIC-initiated sanctions, including memoranda of understanding, delayed or conditional approval of applications, and application denials.

Finally, under recent amendments to HMDA, FDIC examiners will be able to access records kept (Loan Application Register) by the financial institutions, which will disclose all the information previously obtained manually. With the new statutory requirements that the race, sex and income of all applicants and borrowers be supplied by geographic location, as well as the action taken on specific applications, the review of a lender's housing-related lending performance will be widely enhanced and simplified.

Q.4. How many applications have been approved without conditions when the financial institution has had a less than satisfactory rating?

The following table indicates approved CRA-covered applications for the years 1984 through the first half of 1989:

	1984	1985	1986	1987	1988	1st half 1989
Approved	1,580	1,402	1,515	1,750	1,801	839

Without a time-consuming manual review of all application approvals, the FDIC is unable to identify CRA-related conditions attached to approvals. However, in our testimony before the Senate Banking Committee in March of 1988, we stated that no FDIC-supervised institution rated less than satisfactory on the basis of compliance with CRA has had its application approved without agreeing to appropriate corrective actions to favorably resolve FDIC-identified, CRA-related problems. Commitments to corrective actions are usually not as formal as memoranda of understanding or conditional approvals. Institutions not agreeing to such commitments either withdraw their applications or risk denial or approval-with-conditions. Since the Community Reinvestment Act's inception, the FDIC has denied three applications for deposit facilities due to CRA factors.

During the past five years, out of 17 protested applications, one was conditionally approved, 14 were approved without conditions, and two were withdrawn.

Q.5. The March Joint Statement by the Exam Council encourages a dialogue between banks/thrifts and community groups through the expanded CRA statement and public comments thereon. Do you yet know how many banks and thrifts are now writing expanded CRA statements and how many are getting comments from community groups?

It is really too early to estimate the effect of the March Statement. We expect to have data on this within one year. Unfortunately, in the past, we have found that institutions receive few comments for the public file.

Q.6. Describe how and when examiners contact community groups during an exam. How do examiners decide whom to contact? In what percent of exams are community groups interviewed? What are they asked?

In 1980, the FDIC established its outside contact policy. This policy provides that examiners should make the following outside contacts during regular compliance examinations when necessary

to assess the bank's performance in meeting community credit needs under the CRA:

> Any person or organization that has, in a CRA comment to the public file, specifically requested to speak to an examiner;
>
> Any person or organization that has raised a substantial issue in a CRA comment letter which requires further explanation and/or verification -- such persons or organizations should be contacted even where they have not made a specific request for a meeting; and
>
> A representative sample of persons or organizations with whom the lender has said it communicated -- this form of outside contact would normally be made only in circumstances where the examiner or other agency representative determined a need to independently verify the lender's performance in ascertaining local credit needs.

The initial contacts should be made by telephone. A subsequent meeting between the commenter(s) and a designated agency representative may be arranged as necessary. Meetings should be scheduled to accommodate, to every reasonable extent, the commenter's schedule and convenience.

Data is not available as to what percent of examinations include the interviewing of community group representatives. Generally, when contacted, groups are asked about the institution's efforts to communicate with members of its community, including those of low- and moderate-income, regarding the ascertainment of credit needs and the provision of credit services. Examiners also verify communication the institution stated it had with community members.

Q.7. When the Federal Reserve Board reviews an application on CRA grounds, its order on the application routinely includes a discussion of the issues raised, the Board's assessment of the bank's performance with respect to those issues, and how its conclusions affected the final decision. This type of discussion has proved helpful -- to lenders and community groups alike -- in providing insight into the Board's interpretation of CRA. Are the other regulatory agencies willing to follow this practice?

The FDIC issues a formal statement which accompanies an FDIC Order to approve or deny an application. These documents are available to the public. The statement summarizes the FDIC's assessment of the statutory factors that must be resolved prior to approval or denial of an application and its conclusions with respect to any issues raised regarding the CRA and other

protests. Where an application has been protested, the FDIC also sends a letter to the protestants explaining the action taken.

In addition, Section 303.6(g)(2) of the FDIC regulations requires that a summary assessment of an institution's CRA performance be included in the public portion of an application file. This policy has been in effect since 1980. Each summary contains the date of the assessment, a synopsis of assessment results, and a conclusion as to the institution's record of CRA performance.

Q.8. Since there are no performance standards for measuring CRA performance and assigning ratings, what assurance is there that ratings are assigned consistently by different examiners, within different regions of each agency, and across agencies?

The CRA examination procedures and the Interagency CRA Assessment Rating System currently used by the FDIC contain the broad outlines of CRA performance standards. However, judging the CRA performance of an institution is a relative process. This process does not rely on absolute performance standards since the performance of the institution is related to the needs of the community and the ability of the institution to meet those needs. However, because the process is relative does not mean that there are no performance standards. Examiners attempt to review and evaluate a variety of unique complex factors in order to judge an institution's record of CRA performance. The judgment occurs based on a foundation of broad standards set forth in the CRA examination procedures and in the CRA rating system.

Regarding consistency in ratings, ratings must be reviewed by senior level field and regional office examination staff members who have had extensive experience with both safety and soundness and consumer compliance examinations. Moreover, these individuals have interacted with a wide variety of institutions as to size, situation, region, and locale. While the CRA examination process is largely judgmental, FDIC management believes that adequate supervisory oversight serves to limit the potential for rating inconsistencies. The FDIC's examiner training efforts also serve to limit inconsistency through the use of valid and reliable analytical methods and evaluation techniques. The FDIC's Consumer Compliance Coordinator supervisory program is currently being developed, and Compliance Coordinators have now been selected for each of the FDIC's 94 field offices. Periodic, in-depth consumer compliance training will be provided to these specialized Coordinators (for a more extensive explanation of this effort, see the FDIC's July 31, 1989 Senate testimony).

The FDIC strives for consistency with the other agencies by using the Interagency CRA Assessment Rating System and CRA examination procedures developed on an interagency basis. The FFIEC Consumer Compliance Task Force is developing a revised CRA rating system pursuant to FIRREA. The Task Force is also updating the CRA examination procedures as well as developing an interagency training program to implement the revised CRA rating system in 1990.

Q.9. Do financial institutions derive any benefits for achieving a top CRA rating? Should they? What specific recommendations would you have?

The top CRA ratings currently are 1 and 2. Rating (1) indicates that an institution has a strong record of meeting community credit needs; that both the board of directors and management take an active part in the process and demonstrate an affirmative commitment to the community; that an institution receiving this rating normally ranks high in all performance categories, has a commendable record, and needs no further encouragement. Rating (2) indicates that an institution has a satisfactory record of helping to meet community credit needs; that it is ranked in the satisfactory levels of the performance categories; and that it may require some encouragement to help meet community credit needs.

Financial institutions find that satisfactory or better compliance with CRA can prove beneficial. A top rating can prevent complaints and protests which may be costly in terms of application time delays and possible denials, as well as potential adverse publicity. Such a rating also evidences an overall good business relationship between the institution and its community. Thus, we believe institutions with a top CRA rating do realize benefits. We have no specific recommendations.

Q.10. Some banks claim that their CRA ratings have been downgraded because of agency criticism of their documentation. This apparently has occurred even when the bank in question was performing on CRA in a superlative manner. How much new emphasis is being placed on CRA documentation as opposed to performance? How do you balance the two?

Reasonable documentation provides verification of an institution's CRA program and performance. As a party to the revised interagency CRA Statement issued earlier this year, the FDIC supports the emphasis on documentation. The FDIC does not, however, consider this a new focus since reasonable documentation has been stressed throughout the FDIC CRA examination procedures. In the CRA examination procedures, examiners are directed to "ascertain from institution records" certain performance standards, which necessarily calls for

reasonable documentation. Poor documentation practices cause institutions to run unnecessary risks when possible CRA-related problems arise. However, we are unaware of any institution's CRA ratings that have been downgraded due to a lack of or poor documentation.

Q.11. Do agency procedures require examiners to review existing CRA agreements between lending institutions and community groups? If so, describe the procedures. Do examiners routinely assess a financial institution's implementation of such an agreement in evaluating an institution's CRA performance? Do the procedures require examiners to contact the community groups as part of this evaluation?

Examiners are not specifically required to review such CRA agreements. However, to the extent a CRA agreement is involved in an institution's efforts to comply with the CRA or to the extent that an institution requests the activities cited in an agreement to supplement other CRA-related activities, the FDIC examiner will review such activities. This review would determine whether the institution is in fact acting in accordance with the agreement. Examiners are not required to contact any particular community groups in this regard.

Q.12. All of the agencies indicate that HMDA data is integral to CRA evaluations and helps them to determine the degree to which lenders are serving various parts of their communities with respect to mortgage loans. Would comparable data for commercial lending be equally useful? If not, why not?

HMDA was enacted following problems in fair housing lending which were identified by many groups and individuals. Thus far, complaints alleging problems within the area of commercial lending have not materialized. The FDIC, therefore, does not see much value in gathering such data. If a pervasive CRA-related problem were to develop causing potential business borrowers undue hardship, the FDIC would reconsider its stand.

Q.13. A recently released study by the Center for Community Change found that banks and thrifts lend, on average, 3 times as much in white middle class neighborhoods than in minority middle class neighborhoods. Why does this sort of redlining still exist? Should not enforcement of CRA laws stop redlining?

The methodology used to determine these conclusions must be scrutinized for validity and reliability. Assuming the methodology is reliable, causative variables must then be determined and tested since correlation does not necessarily mean causation. One critical factor to investigate would be loan demand data. Information on applicant denials, not currently available to the public, may contain pertinent explanatory information. For example, there may be significant

numbers of applicants rejected for reasons such as poor credit history, insufficient income, unacceptably high debt-to-income ratio, etc. The Department of Justice (DOJ) is currently undertaking an extensive analysis of lending data from a number of lending institutions in one large urban area to better understand the underlying reasons for correlations indicating possible lending bias. The FDIC hopes to meet with DOJ staff to discuss the results of these research efforts when they are completed.

Effective enforcement of the ECOA, HMDA, CRA and the Fair Housing Act should help prevent illegal redlining. The FDIC receives very few fair housing complaints. Should an enforcement problem be determined to exist based on indications from DOJ research or other sources, the FDIC will take appropriate action.

Q.14. Each agency's testimony provided data on how many hours examiners spend per CRA exam. Clarify your methodology, as it is uncertain whether each agency followed the same methodology in calculating the hours.

The FDIC provided the following information to the subcommittee in July of 1989 regarding examiner hours spent per CRA exam.

> Actual hours spent on CRA examinations may relate more to the type of institution (e.g., commercial vs. savings institution, wholesale vs. retail) than to asset size. For special CRA examinations which are conducted in response to an institution application or a protest, the number of hours expended may be higher than average. The following Table shows the average number of hours spent per examination on CRA compliance matters:

Average Hours Expended Per Examination on CRA from 1985 through 1988 by Asset Size of Bank

Average Hours Per Exam	$0-50 million	$50-100 million	$100-500 million	Over $500
1985	4 1/2	6	10 1/2	24 1/2
1986	5	6 1/2	8	29
1987	5	5 1/2	8	16 1/2
1988	5	6 1/2	9	22

The FDIC used an average where the total number of hours expended was divided by the number of institutions examined. We computed the figures by asset size in order to capture the variations by size. The numbers represent hours spent examining for compliance with the CRA and HMDA. These figures would increase if hours spent on examining for compliance with the Fair Housing Act and Equal Credit Opportunity Act were included.

Q.15. The FDIC's testimony lists the possible enforcement actions as unsatisfactory ratings, corrective advisements and memoranda of understanding, application denials, and cease and desist orders. Since only two percent of FDIC-supervised banks get unsatisfactory ratings and no applications have been denied in the past five years, what evidence is there of strong CRA enforcement? How frequently have corrective advisements, memoranda of understanding, and cease and desist orders been issued?

Evidence of strong FDIC enforcement of CRA includes the following: satisfactory or better CRA and compliance composite ratings for the large majority of FDIC-supervised banks and the receipt of few complaints, protests and telephone complaints and inquiries.

The following table indicates, by two-year increments, FDIC measures to enforce compliance with consumer and civil rights mandates (corrective advisements were not included in our final testimony):

	1980	1982	1984	1986	1988
Number of Compliance Examinations	6,305	5,359	1,881	1,228	3,066
Number of Compliance Visitations	471	426	296	101	992
*Number of Memoranda of Understanding pertaining to Consumer Compliance	9	27	72	45	123
*Number of Cease and Desist Orders pertaining to Consumer Compliance	3	3	1	1	3

*May not always involve CRA

Note: Each examination report is sent to institution management accompanied by a supervisory letter requiring a response.

The decrease from 1980-1986 in the number of consumer compliance examinations occurred partially because of the substantial increase in the number of problem banks and partially because of a 1978 FDIC policy decision to reduce the number of bank examiners. At that time, we thought that our regulatory responsibilities could be accomplished with fewer traditional on-site examinations, especially for banks with satisfactory ratings. To supplement our reduced examination efforts, we used increased offsite surveillance, brief visitations, reliance on

state regulators where appropriate, and increased market discipline. Although that level of supervision may have been appropriate at the time, conditions subsequently changed. During the past four years, we have increased our staff substantially and will continue to do so. We are dedicated to reestablishing a strong and credible program for consumer compliance examinations and enforcement within our established supervision division.

Q.16. The FDIC's testimony states, "The goal is to examine banks rated 4 and 5 for compliance at least every 12 months, and banks rated 1, 2, or 3 at least every 24 months, with visitations conducted as necessary." What is the actual frequency of CRA examinations?

The above-mentioned frequency goals for compliance examinations went into effect in the latter part of 1988. The following is an aging schedule for FDIC regulated institutions examined for compliance, including CRA, on or prior to March 31, 1989. We do not have a separate agency schedule just for CRA examinations.

Number 1 & 2* rated institutions	Exams 0-2yrs. old	Number 3 rated institutions	Exams 0-2yrs. old	Number 4 & 5* rated institutions	Exams 0-1yr. old
9,038	4,537(50%)	1,010	622(62%)	62	25(40%)

* Composite consumer compliance rating.

We should explain however, that recently notable safety and soundness problems in the industry have caused some diversion of resources from consumer compliance examinations. With increasing resources, renewed emphasis is being placed on compliance examinations and meeting our examination frequency goals.

Q.17. In the past five years no application has been conditionally approved by the FDIC, except for one of the applications protested. If an institution complies with CRA, it does not need conditions attached to its application just because a protest has occurred. If an institution does not comply with CRA, then conditions should be added or the application denied whether or not a protest occurs. Explain why more nonprotested applications are not conditionally approved?

Again, we are not aware of any FDIC-supervised institution rated less than satisfactory on the basis of compliance with the CRA that has had an application approved without agreeing to appropriate corrective actions to favorably resolve FDIC identified, CRA-related problems. Most situations do not require the attachment of conditions; however, the FDIC has

that important option available which it has chosen to use sparingly. Almost always, FDIC-supervised institutions with CRA-related problems called to their attention by examiners move to correct such problems in a timely manner.

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